Supreme Court, U.S.
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No. __-____

IN THE
Supreme Court of the United States

NANOPIERCE TECHNOLOGIES, INC. (N/K/A VYTA CORP.), KATHY-KNIGHT MCCONNELL, HELEN KOLADA, MAUREEN O'SULLIVAN, JANE SEITZ, STEPHEN SEITZ, AND JAMES STOCK,
Petitioners,
v.

DEPOSITORY TRUST AND CLEARING CORPORATION, DEPOSITORY TRUST COMPANY, AND NATIONAL SECURITIES CLEARING CORPORATION,
Respondents.

On Petition for a Writ of Certiorari to the Supreme Court of Nevada

PETITION FOR A WRIT OF CERTIORARI

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February 4, 2008

QUESTION PRESENTED

Whether state-law claims alleging misrepresentations and omissions by securities transaction clearing agencies are conflict preempted, even though nothing in federal law requires or permits those entities to engage in misrepresentations or omissions to the public, and federal securities law seeks to ensure full and fair disclosure to the investing public.

LIST OF PARTIES TO THE PROCEEDINGS

Petitioners NanoPierce Technologies, Inc. (n/k/a Vyta Corp.), Kathy-Knight McConnell, Helen Kolada, Maureen O'Sullivan, Jane Seitz, Stephen Seitz, and James Stock were the plaintiffs in the Nevada district court proceedings and the appellants in the Nevada Supreme Court proceedings.

Respondents Depository Trust and Clearing Corporation, Depository Trust Company, and National Securities Clearing Corporation were the defendants in the Nevada district court proceedings and the respondents in the Nevada Supreme Court proceed-

CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6 of the Rules of this Court, petitioner NanoPierce Technologies, Inc. (n/k/a Vyta Corp.) states the following:

In January 2006, NanoPierce Technologies, Inc. changed its name to Vyta Corp., a Nevada corporation. Vyta Corp. has no parent company, and no publicly held company owns 10% or more of Vyta Corp.'s stock.

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NanoPierce Technologies, Inc. (n/k/a Vyta Corp.), Kathy-Knight McConnell, Helen Kolada, Maureen O'Sullivan, Jane Seitz, Stephen Seitz, and James Stock respectfully petition for a writ of certiorari to review the judgment of the Supreme Court of Nevada in this case.

OPINIONS BELOW

The opinion of the Supreme Court of Nevada (Pet. App. 1a-27a) is reported at 168 P.3d 73. The opinion of the Nevada district court (Pet. App. 28a-32a) is not reported.

JURISDICTION

The Supreme Court of Nevada entered its judgment on September 20, 2007. A petition for rehearing was denied on November 5, 2007. *See* Pet. App. 33a-35a. On December 14, 2007, Justice Kennedy extended the time within which to file a petition for a writ of certiorari to and including February 4, 2008. *See id.* at 57a. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(a).

STATUTORY PROVISIONS INVOLVED

Relevant provisions of the Securities Exchange Act of 1934, 15 U.S.C. § 78a *et seq.*, and the Securities Act of 1933, 15 U.S.C. § 77a *et seq.*, are set forth at Pet. App. 36a-56a.[1]

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[1] Provisions of the Securities Exchange Act of 1934 and the Securities Act of 1933 are all codified in Title 15 of the United States Code and are cited herein simply as, for example, "§ 78q-1".

INTRODUCTION

Respondents are the major entities that perform the back-office tasks of clearing and settling securities transactions, which occur after the parties and their brokers have agreed on terms. Petitioners are a publicly traded small company and several of its individual investors who lost substantial monies as a result of respondents' misrepresentations and omissions to the public regarding their clearing and settlement activities.

For more than a century, investors have brought claims under state law when a defendant failed properly to uphold its obligation to clear or settle a securities transaction. In 1975, Congress passed legislation permitting the Securities and Exchange Commission ("SEC" or "Commission") to register clearing agencies, and it prohibited unregistered clearing agencies from performing clearing and settlement functions. The SEC-approved rules that are relevant here for the respondent clearing agencies span only three pages, and nowhere in those rules or elsewhere in federal law are respondents required or permitted to mislead the public about their clearing and settlement activities through either affirmative misrepresentations or omissions. Nor did Congress express any intent to preempt such claims; rather, it left unaffected the savings clause enacted in 1934 precisely to preserve such claims and inserted two additional savings clauses to make clear its intention to preserve much of state law affecting clearing agencies.

Yet a majority of the Nevada Supreme Court below – over a powerful dissent – too quickly acceded to respondents' broad-brush claims that federal regulation of clearing agencies is equivalent to a conflict with federal law that somehow preempts state-law

claims alleging misrepresentation about respondents' clearing activities. The Nevada Supreme Court's decision conflicts directly with a decision of the Delaware Supreme Court regarding the preemptive effects of the rules of self-regulatory agencies, as well as with other decisions of the federal courts of appeals and state courts of last resort.

Moreover, that decision also conflicts with *Bates v. Dow AgroSciences LLC*, 544 U.S. 431 (2005), in which this Court soundly reversed an overwhelming tide of lower court decisions finding preemption of state law by a federal statute governing pesticides, explaining that the lower courts had not been careful enough in their analysis. As the Nevada Supreme Court's dissenters pointed out below, the specific analysis and reasoning in *Bates* should have been controlling here in important respects and compels a finding that there is no conflict preemption. The lower courts' misunderstanding of *Bates* – now three years after this Court's decision – demonstrates the need for this Court's additional guidance on the proper articulation and application of conflict-preemption principles. This case raises important concerns about the federal and state policies of full disclosure that govern securities regulation and is an appropriate vehicle for the Court to clarify the conflict-preemption principles that the lower courts must regularly apply.

In the alternative, if this Court does not grant review at this time, it should hold this case for disposition in light of *Altria Group, Inc. v. Good*, No. 07-562, which presents a similar question about the extent to which alleged federal approval of a regulated activity bars state-law claims for misrepresentations concerning that activity.

STATEMENT OF THE CASE

1. More than 150 years ago, the States initiated the first efforts to ensure the integrity of this country's financial markets. *See* 1 Louis Loss & Joel Seligman, *Securities Regulation* 31-43 (3d ed. 1998) ("*Securities Regulation*"); Gerald D. Nash, *Government and Business: A Case Study of State Regulation of Corporate Securities, 1850-1933*, 38 Bus. Hist. Rev. 144, 144-52 (1964) ("*1850-1933 Case Study*"); Louis Loss & Edward M. Cowett, *Blue Sky Law* 3-17 (1958) ("*Blue Sky Law*"). State supervision of the securities industry began as an aspect of the States' traditional regulation of corporations and other business associations. As the number of corporations increased in the middle of the nineteenth century, States responded by passing targeted legislation directly regulating certain types of issuers of securities. *See 1850-1933 Case Study* at 148-49; 1 *Securities Regulation* at 31-32. In 1911, Kansas passed the first "comprehensive licensing system" for the securities industry, one of many state statutes now referred to as "Blue Sky Laws." *See Blue Sky Laws* at 7-9. By 1933, every State but one had enacted such a statute. *See id.* at 10; 1 *Securities Regulation* at 40; *see also 1850-1933 Case Study* at 150-52.

"In the wake of the 1929 stock market crash and in response to reports of widespread abuses in the securities industry," Congress passed "two landmark pieces of securities legislation": the Securities Act of 1933 ("1933 Act") and the Securities Exchange Act of 1934 ("1934 Act"). *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 170-71 (1994). Recognizing that the States, because of jurisdictional impediments and resource deficiencies, lacked the ability to ensure the optimal level of

disclosure nationwide, *see* 1 *Securities Regulation* at 146-51, 219, Congress in the 1933 and 1934 Acts instituted a national regime of mandatory corporate disclosure, *see, e.g.*, § 78j(b) (general antifraud provision making it unlawful "[t]o use or employ, in connection with the purchase or sale of any security . . . , any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe"); 17 C.F.R. § 240.10b-5 (SEC implementing Rule 10b-5, adopted in 1942).

When Congress entered the field of securities regulation in 1933 and 1934, it chose not to displace the existing state systems of securities regulation. The 1933 and 1934 Acts each explicitly preserved applicable state law. *See* 1933 Act § 16, 48 Stat. 74, 84; 1934 Act § 28, 48 Stat. 881, 903. The States have continued their traditional role of protecting investors. "Today all 50 states, the District of Columbia, Guam, and Puerto Rico have blue sky laws in force," with most having adopted the Uniform Securities Act of 1956 and several more the Revised Uniform Securities Act of 1985. 1 *Securities Regulation* at 41-42. State statutes and common law provide significant private remedies for investors harmed by misrepresentation and other misconduct. *See* 9 *id.* at 4114-66. "Congress plainly contemplated the possibility of dual litigation in state and federal courts relating to securities transactions." *Matsushita Elec. Indus. Co. v. Epstein*, 516 U.S. 367, 383 (1996).

2. Clearance and settlement, including the actual transfer of securities certificates from seller to buyer, are so-called "back-office" functions that must be performed for each securities transaction. Clearance is the process of verifying and confirming the terms of the trade, such as the number of shares, price, buyer,

and seller. After a trade clears, it settles on the date prescribed by regulation, when the seller delivers the shares and the buyer delivers payment. If the seller does not deliver the shares on the settlement date, the industry deems it a "fail to deliver." State law has long been the primary, if not exclusive, regulator of clearance and settlement functions. *See* 6 *Securities Regulation* at 2912 ("the securities transfer and clearance process [was] a subject previously left to state law").

For example, state-law claims have regularly been adjudicated against fails to deliver, fraud, misrepresentation, or other actionable conduct or omissions in the clearance and settlement of securities.[2] And the

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[2] *See, e.g., Olde Monmouth Stock Transfer Co. v. Depository Trust & Clearing Corp.*, 485 F. Supp. 2d 387, 397-98 (S.D.N.Y. 2007) (allowing state-law claim for tortious interference to proceed against clearing corporations DTCC and DTC, which are respondents here); *Goldstein v. Depository Trust Co.*, 717 A.2d 1063, 1064 (Pa. Super. Ct. 1998) (DTC's motion to compel arbitration denied in suit brought under state law for breach of fiduciary duty arising from DTC's failure to segregate and account for interest owed on funds paid for shares), *appeal denied*, 736 A.2d 605 (Pa. 1999); *Smith Barney, Harris Upham & Co. v. Liechtensteinische Landesbank*, 866 F. Supp. 114, 117 (S.D.N.Y. 1994) (where DTC "operating procedures" contained no "precise time within which DTC is required to give notice of cancellations or confiscations of securities deposited with DTC," holding that the applicable standard was a "reasonable time" as provided under state common law); *In re Weiss Sec., Inc.*, 542 F.2d 840 (2d Cir. 1976) (denying DTC predecessor's complaint to reclaim securities it had transferred to insolvent company); *Travis Inv. Co. v. Harwyn Publ'g Corp.*, 288 F. Supp. 519 (S.D.N.Y. 1968) (adjudicating state-law claim against transfer agent for failure to transfer shares); *People v. Ruskay*, 152 N.E. 464 (N.Y. 1926) (under New York law and exchange's clearing and settlement procedures, broker's criminal conviction could not be sustained).

Uniform Commercial Code ("UCC") has long governed clearance and settlement of securities.[3] "The original version of [UCC] Article 8, drafted in the 1940s and 1950s, was based on the assumption that possession and delivery of physical certificates are the key elements in the securities holding system. Ownership of securities was traditionally evidenced by possession of the certificates, and changes were accomplished by delivery of the certificates." Lary Lawrence, *Anderson on the Uniform Commercial Code* 596 (3d rev. ed. 2005) ("*Anderson on the UCC*").

3. In the late 1960s and early 1970s, however, the securities industry suffered a "back office paper crunch" due in part to the need to physically transfer stock certificates, continually increasing trading volumes, and the failure of disparate and largely manual clearance and settlement systems to work together effectively. 6 *Securities Regulation* at 2914; *see* S. Rep. No. 94-75, at 5 (1975), *reprinted in* 1975 U.S.C.C.A.N. 179, 183-84. As a result, "many purchasers never actually received their stock certificates nor sellers their money"; and numerous brokers, "faced with liability for these incomplete transactions, went bankrupt." *Bradford Nat'l Clearing Corp. v. SEC*, 590 F.2d 1085, 1091 (D.C. Cir. 1978).

In 1975, Congress enacted the Securities Acts Amendments of 1975, Pub. L. No. 94-29, 89 Stat. 97 ("1975 Amendments"), which addressed multiple issues including but not limited to the back-office crisis. To address that crisis, and in recognition of new data processing and communications techniques,

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[3] *See, e.g., Delaware v. New York*, 507 U.S. 490, 504-05 (1993) (UCC and additional state laws governed determination that depositories and other intermediaries holding securities were "debtors" for purposes of interstate escheat claims).

Congress added § 17A to the 1934 Act, codified at 15 U.S.C. § 78q-1. The Senate Subcommittee on Securities had identified two primary causes of the back-office crisis in securities clearance and settlement: the absence of "a nationwide system for the clearance and settlement of securities transactions" and a "lack of uniformity and coordination among the various methods and systems of clearing and settlement." S. Rep. No. 94-75, at 54, *reprinted in* 1975 U.S.C.C.A.N. 232. Another congressional study concluded that "[c]omplete elimination of the stock certificate is the ultimate goal in modernizing the securities processing system." H.R. Rep. No. 92-1519, at 70 (1972); *see generally* 6 *Securities Regulation* at 2919-22.[4]

Accordingly, Congress "directed" the SEC in § 78q-1 "to facilitate the establishment of a national system for the prompt and accurate clearance and settlement of transactions in securities." § 78q-1(a)(2)(A)(i). Congress authorized the SEC to register and regulate clearing agencies, and it prohibited unregistered clearing agencies from doing business in interstate commerce. *See* § 78q-1(b).[5] The statute also directed

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[4] Following the 1975 Amendments, state laws incorporating UCC Article 8 were revised to reflect that, in most future cases, "ownership of securities would not be evidenced by physical certificates." *Anderson on the UCC* at 597. In particular, the state-law UCC revision provides that "a person acquires a security entitlement if a securities intermediary . . . [i]ndicates by book entry that a financial asset has been credited to his securities account." Nev. Rev. Stat. § 104.8501.2(a). The UCC further defines a "securities intermediary" to include a "clearing corporation" – that is, a "person that is registered as a 'clearing agency' under the federal securities laws." *Id.* § 104.8102(e)(1), (m).

[5] Registered clearing agencies, like securities exchanges, are treated in the 1934 Act as self-regulatory organizations. *See* § 78c(a)(26).

the Commission "to end the physical movement of securities certificates in connection with the settlement among brokers and dealers of transactions in securities." § 78q-1(e). In all respects, Congress charged the SEC to exercise its authority under § 78q-1, "having due regard for the public interest, the protection of investors, the safeguarding of securities and funds, and maintenance of fair competition among brokers and dealers, clearing agencies, and transfer agents." § 78q-1(a)(2)(A).

Section 78q-1 does not address claims concerning clearing or settlement under either state or federal law. The 1975 Amendments, however, left intact both (i) the savings clause of the 1934 Act, which provides that the rights and remedies in the Act "shall be in addition to any and all other rights and remedies that may exist at law or in equity," § 78bb(a); and (ii) the implied private right of action long held by the courts to exist under section 10(b) of the 1934 Act and SEC Rule 10b-5. Thus, nothing in the 1975 Amendments altered the long-established dual system of remedies.

Moreover, the 1975 Amendments made clear, in two internal savings clauses, that clearing and settlement activities are not above the States' authority. *First*, Congress provided that "[n]othing in this section [78q-1] shall be construed to impair the authority of any State banking authority or other State or Federal regulatory authority . . . to make and enforce rules governing [clearing agencies] which are not inconsistent with this chapter and the rules and regulations thereunder." § 78q-1(d)(4).[6]

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[6] *See* 6 *Securities Regulation* at 2926-27 ("Because so many transfer agents and clearing agencies are banks, a political compromise (reminiscent of the 1964 adoption of § 12(i) with

Second, Congress made clear that States are not limited to regulating in ways "not inconsistent" with federal law (*id.*), but may even adopt certain inconsistent rules that *override* the SEC's own rules. In a 1990 amendment, Congress first authorized the SEC, "[n]otwithstanding any provision of State law," to adopt rules concerning both "(A) the transfer of . . . securities" and "(B) rights and obligations of purchasers, sellers," and others "involved in or affected by such transfers," provided that the SEC first makes three findings justifying displacement of state law. § 78q-1(f)(1); *see* § 78q-1(f)(2) (setting out required findings). Nevertheless, Congress then provided what might be called a reverse preemption or clawback power to the States, enabling them to promulgate "a provision that differs from that applicable under the Commission's rule." § 78q-1(f)(3); *see* 6 *Securities Regulation* at 2928 ("[t]hose who drafted this part of the 1990 Act clearly realized that they were walking on eggs" in venturing into this "traditionally state law area").

4. Pursuant to § 78q-1, the SEC registered a number of clearing agencies, including respondents here. In particular, the SEC authorized respondents Depository Trust Company ("DTC") and National Securities Clearing Corporation ("NSCC") to provide automated clearance and settlement of virtually all broker-to-broker securities transactions. DTC

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respect to the registration of bank securities) split jurisdiction between the SEC and the federal bank regulators . . . with respect to transfer agents and clearing agencies that are banks.") (footnote omitted). Although Professor Loss's treatise statement focuses on federal banks and banking authorities, the savings clause itself is not so limited. *See* § 78q-1(d)(4) ("any State banking authority *or other State or Federal regulatory authority*") (emphasis added).

and NSCC, in turn, are wholly owned subsidiaries of respondent Depository Trust and Clearing Corporation ("DTCC").[7] DTCC "is owned by its principal users," which include some 600 "international broker/dealers, correspondent and clearing banks, mutual fund companies and investment banks," as well as its "preferred shareholders," the National Association of Securities Dealers ("NASD") and the New York Stock Exchange ("NYSE").[8] The profits made by DTCC, including its subsidiaries, inure to the benefit of the industry participants that own and use it.[9] In addition, the more transactions processed by DTCC, the more commissions are earned by its industry participant owners and operators.[10]

Respondent DTC's role is to eliminate the movement of paper stock certificates. It acts as a securities depository; changes in stock ownership are electronically recorded in brokers' respective DTC accounts, and there is no physical transfer of security certificates held by DTC. Share owners may in theory demand possession of their certificates – though they must go through their brokers to do so, which is not a quick process. As a practical matter,

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[7] *See* http://www.dtcc.com/about/subs/.

[8] *See* http://www.dtcc.com/about/business/customers.php; DTCC, *Annual Report 2006*, at 50 (2007), *available at* http://www.dtcc.com/downloads/annuals/2006/2006_report.pdf; *Anderson on the UCC* at 598.

[9] *See* http://www.dtcc.com/about/business/customers.php ("As an industry-owned corporation, DTCC and its subsidiaries operate on an 'at-cost basis,' charging transaction fees for services and then returning excess revenue to its members.").

[10] *See, e.g.*, Merrill Lynch & Co., Inc., Quarterly Report (Form 10-Q), at 5, 70 (Nov. 7, 2007) (commissions constituted largest single source of revenues for reported period), *available at* http://ir.ml.com/sec.cfm?DocType=&Year=2007.

therefore, DTC holds the vast bulk of certificates issued by publicly traded companies.

Although the use of a common depository eliminates the need for physical deliveries, an enormous number of entries would still have to be made on DTC's books if each transaction between its participants were recorded one by one. Respondent NSCC (which acts as an intermediary between DTC and brokers) streamlines the necessary accounting functions with its "Continuous Net Settlement" system by recording only the net changes in the positions of each participant at the end of each day. For example, if Broker A in a given day effects numerous individual transactions, purchasing 20,000 shares and selling 10,000 shares of company XYZ, then NSCC will instruct DTC to show that Broker A's DTC account reflects a net gain of 10,000 shares of XYZ for that trading day.

When the SEC registered DTC and NSCC as clearing agencies pursuant to § 78q-1, it expressly stated that state-law standards of care would continue to apply to their conduct in handling securities. Thus, the SEC provided that DTC and NSCC "are each responsible under state or federal law, or both, to protect participants' securities and funds." Order, *Depository Trust Co., et al.*, SEC Release No. 20,221, 48 Fed. Reg. 45,167, 45,179 (Oct. 3, 1983); *see also id.* (declining to impose a "unique federal standard of care for registered clearing agencies").

5. SEC rules typically require stock trades to clear within three (formerly five) business days; that is, the buyer pays the seller and the seller delivers shares to the buyer by the settlement date prescribed by federal law. *See* 17 C.F.R. § 240.15c6-1. When a broker sells more shares than it has on account at

DTC and fails to deliver within the standard three-day clearance period, the buying broker's two traditional remedies have been either to buy those shares in the open market (with the selling broker being responsible for any price increase) or simply to wait for the shares to become available as other transactions are cleared through NSCC.

In 1981, the SEC authorized a third option known as the stock borrow program. That program permits willing brokers unrelated to a transaction to lend (their customers') shares from the broker's DTC or NSCC account. NSCC then credits the borrowed shares to the buying broker's account through an automated system that matches lenders with buyers. The stock borrow program was designed to cure short-term delivery failures by sellers of securities. Although NSCC's rules currently span more than 300 pages, only three pages concern the stock borrow program.[11]

6. Petitioners are NanoPierce Technologies, Inc. ("NanoPierce"), a small Nevada corporation traded on the NASDAQ Over the Counter Bulletin Board, along with several of its individual shareholders.[12] Petitioners brought suit in Nevada state court, alleging that respondents misrepresented the effects of the stock borrow program and caused market manipulation.

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[11] *See* NSCC Rules & Procedures, Addendum C (NSCC Automated Stock Borrow Program Procedures), *available at* http://www.dtcc.com/legal/rules_proc/nscc_rules.pdf.

[12] NanoPierce was renamed Vyta Corp. in January 2006, but Vyta has not been formally substituted as the named plaintiff in the Nevada state courts. Because the court decisions and pleadings below all refer to NanoPierce, we retain that nomenclature here for the convenience of the Court.

Petitioners' amended complaint alleges that, despite the stock borrow program's purported development in order to cure short-term failures to deliver, respondents have misrepresented and misused the program so as to permit failures to deliver to remain uncured for months and even years. Such omissions and misrepresentations have facilitated the abusive practice of "naked" short selling, whereby unscrupulous short sellers can rapidly drive down the price of a company's shares. In a traditional short sale, the seller sells shares it has first arranged to borrow (typically from a broker) and thus has the shares available to deliver to the buyer on the settlement date. A "naked" short sale is so named because the seller sells the shares *without* borrowing the stock, and thus fails to deliver those shares on the settlement date.[13]

NSCC uses the automated stock borrow program to supply the shares the seller has failed to deliver to the buyer, either because of a naked short sale or for any other reason. The fail to deliver is not thereby cured, however; the seller still owes the shares, but it (via its broker's participation in the stock borrow program) owes them to NSCC rather than the buyer.[14] Both the lending and buying brokers thus effectively "own" the same shares in their DTC accounts; and their customer statements will each reflect owner-

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[13] In selling a stock short, whether in a naked or traditional sale, the seller is betting that the price of the stock will drop before it has to go into the market and buy replacement shares to repay the lender.

[14] *See* http://www.dtcc.com/about/business/tplus3.php ("NSCC steps into the middle of a trade and assumes the role of central counterparty, taking on the buyer's credit risk and the seller's delivery risk.").

ship of the borrowed and delivered shares, but without indicating that the other broker's customer has ownership rights to the very same shares. Moreover, the buyer's broker may make those same shares available for lending in the stock borrow program, with the potential result that not only two investors, but potentially three or more – a potentially unlimited number – are deemed to own the same shares.

The effect of this scheme has been to create millions of unregistered "phantom" shares that artificially increase the electronic supply of the issuers' shares in the marketplace and are not backed by a stock certificate on deposit at DTC. That oversupply of phantom shares drives down the price of the stock and decreases the value of existing shareholders' holdings. For a small capitalization company like NanoPierce, the effect can be devastating because the artificially increased supply of phantom shares in the market materially drives down the price of the stock. Respondents have a strong incentive to continue permitting this practice in order to generate fees, and their industry-participant members likewise benefit from the commissions they receive from their clients for processing naked short sales. *See supra* p. 11 & n.10.

Petitioners allege that respondents have misrepresented these effects of the stock borrow program. Fundamentally, respondents have denied and failed to disclose that the real effect of their operation of the stock borrow program is to create phantom shares that dilute the value of validly issued shares. For example, petitioners allege that respondents have misrepresented that the artificial shares created by the stock borrow program are issued and outstanding shares of NanoPierce. *See* Pet. App. 20a-21a. And

respondents have made misrepresentations about the efficacy of the program as a prompt and accurate settlement mechanism, without disclosing the critical fact that it injects phantom shares into the marketplace, creating artificial oversupply that dilutes the value of a company's stock. *See id.* at 19a-20a. At the same time, respondents have failed to disclose the fact that there have long been significant numbers of fails to deliver in their system, thus diluting the share value of NanoPierce and other firms' securities. Nothing in the SEC's rules permits or requires respondents to misrepresent or fail to disclose that the net effect of the stock borrow program is to create phantom shares – a material fact that respondents had long concealed and have continued to deny throughout this litigation.

Indeed, after this case was filed, SEC Chairman Christopher Cox noted "the serious problem of abusive naked short sales, which can be used as a tool to drive down a company's stock price," and stated that the SEC is "concerned about persistent failures to deliver in the market for some securities."[15]

7. The Second Judicial District Court of Washoe County, Nevada, held petitioners' claims preempted, without stating whether its decision was based on field preemption, conflict preemption, or both. *See* Pet. App. 30a-32a.

On direct review, the Nevada Supreme Court first rejected respondents' reliance on the doctrine of field preemption. *See id.* at 10a-15a. Relying on the savings clauses in both the 1934 Act and the 1975 addi-

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[15] Christopher Cox, Opening Statements at the Commission Open Meeting (July 12, 2006), *at* http://www.sec.gov/news/speech/2006/spch071206cc2.htm.

tion of § 78q-1, the court concluded that "Congress explicitly left room for state laws to supplement the federal regulatory scheme and thus did not reveal a 'clear and manifest' intent to occupy the field of regulating clearing agencies." *Id.* at 14a-15a.

A majority of the Nevada Supreme Court, however, proceeded to find petitioners' claims barred under principles of conflict preemption. The court initially recognized that Congress's intent to preempt state-law claims "must be 'clear and manifest,'" and that there is a "strong presumption that areas historically regulated by the states generally are not superseded by a subsequent federal law." *Id.* at 8a-9a (quoting *Bates*, 544 U.S. at 449). But the court concluded that petitioners' claims are "inextricably entwined with an assertion that respondents have violated their own Commission-approved rules governing the Stock Borrow Program." *Id.* at 17a.

Two justices dissented in part, concluding with respect to petitioners' misrepresentation-based claims that petitioners "are not directly challenging any NSCC rule's language, but rather that respondents represent that they satisfy buy-in requests by purchasing shares in the open market, while instead using the Stock Borrow Program to satisfy buy-in requests." *Id.* at 26a. The dissenters relied on *Bates*'s holding that state-law claims not inconsistent with federal requirements are not preempted:

> Determining whether respondents are liable on state law grounds for inaccurately representing how they executed buying brokers' notifications to purchase shares on the open market is not inconsistent with the Commission's approval of the Stock Borrow Program or the NSCC's rules, even if it indirectly

> causes respondents to choose whether to change those rules or face potential additional lawsuits.

Id. (citing *Bates*, 544 U.S. at 445).[16]

REASONS FOR GRANTING THE PETITION

This case arises in the context of overlapping state and federal securities laws that serve a common purpose: to protect investors by ensuring appropriate transparency and full disclosure of relevant information, and, by so doing, to safeguard the integrity of the securities market. As this Court has explained, the federal securities laws "'substitute a philosophy of full disclosure for the philosophy of *caveat emptor* and thus . . . achieve a high standard of business ethics in the securities industry.'" *Affiliated Ute*

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[16] The SEC filed an *amicus* brief with the court below urging conflict preemption, based largely on the assertion that petitioners are simply wrong to suggest that the stock borrow program creates artificial or phantom securities. *See* Brief of the Securities and Exchange Commission, *Amicus Curiae*, on the Issue Addressed at 14-16, 22-27 (Nev. filed Feb. 2, 2006). The SEC did so, however, by claiming only that NSCC's accounting system does not accurately "reflect *ownership positions*," pointing out that the "number of securities issued and outstanding is determined by the security issuer." *Id.* at 14-15. At the same time, however, the SEC conceded the correctness of petitioners' claim that the *electronic universe* of shares available for trading can be much larger:

> While the number of securities outstanding does not change because of the clearance and settlement system, the aggregate number of positions reflected in customer accounts at broker-dealers may in fact be *greater* than the number of securities issued and outstanding.

Id. at 16 n.6 (emphasis added). *Accord* Proposed Rule, *Short Sales*, 68 Fed. Reg. 62,972, 62,975 (Nov. 6, 2003) ("At times, the amount of fails to deliver may be greater than the total public float.").

Citizens of Utah v. United States, 406 U.S. 128, 151 (1972) (quoting *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 186 (1963)). Through the savings clause in the 1934 Act, § 78bb(a), Congress has recognized that state law can further these purposes by providing important remedies for investors who have been deceived or misled. In this case, petitioners' state-law claims – which seek only to ensure that respondents accurately inform the market generally, and their customers specifically, of their actual business practices in administering their stock borrow program[17] – further the federal policies of transparency and investor protection and do not impede the proper functioning of any federal regulatory mechanism.

Nevertheless, the Nevada Supreme Court has held that, because the SEC has approved the rules that govern the functioning of respondents' stock borrow program, Nevada law "'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress,'" *Crosby v. National Foreign Trade Council*, 530 U.S. 363, 372-73 (2000) (quoting *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941)), to the extent that a state-law claim authorizes recovery for misrepresentations in connection with that program. *See* Pet. App. 20a & n.46. That decision directly conflicts with a decision of the Delaware Supreme Court concerning the extent to which

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[17] Petitioners' complaint contained several additional claims based not on misrepresentations or omissions by respondents, but on other violations of state law by respondents. These additional claims were also dismissed by the state courts. *See* Pet. App. 21a-23a. Although the state supreme court's judgment was erroneous in its entirety, petitioners seek review in this Court of that judgment only insofar as it affirmed the dismissal of their claims based on misrepresentations or omissions.

the SEC-authorized regulations of self-regulatory organizations preempt state-law claims for misrepresentation; deepens an existing and broader conflict concerning the appropriate treatment of misrepresentations in connection with federally authorized activities; and conflicts with this Court's decision in *Bates*, among other decisions of this Court. Review is warranted for all of these reasons. It is also warranted because of the national importance of the question whether the federal and state policies of full disclosure in the securities markets will apply to what the court below termed an "exploitable flaw" (*id.* at 20a) in respondents' system. In the alternative, if this Court does not grant review at this time, it should hold this case for disposition in light of *Altria Group, Inc. v. Good*, No. 07-562, which presents a similar question about the extent to which alleged federal approval of a regulated activity bars state-law claims for misrepresentations concerning that activity.

I. PLENARY REVIEW IS WARRANTED BY THE CONFLICTS CREATED BY THE DECISION BELOW AND ITS IMPORTANCE TO THE NATIONAL SYSTEM OF SECURITIES REGULATION

A. The Decision Below Conflicts With Decisions Of Other State Courts Of Last Resort And Federal Courts Of Appeals

1. The decision below directly conflicts with *O'Malley v. Boris*, 742 A.2d 845 (Del. 1999). The Delaware Supreme Court there addressed the preemptive effect of a rule of NASD – a self-regulatory organization that is one of respondent DTCC's preferred shareholders. A "negative response letter" is a notification to a broker's client that a change to the

client's account will be made unless the client objects. *Id.* at 847. The defendants in *O'Malley* claimed that an NASD rule authorizing the use of such letters for certain accounts preempted a state-law claim that a broker's notification to its clients was misleading because it failed to disclose the broker's interest in the transaction. *Id.* at 848. The rule "specifie[d] the information . . . [to] be included in such a letter," and the SEC had approved the NASD rule to enhance the "'timely and efficient execution of . . . bulk exchanges without compromising investor protections.'" *Id.* at 848 (quoting SEC Release No. 31,558, 57 Fed. Reg. 58,525, 58,526 (Dec. 10, 1992)) (second ellipsis in original).

The *O'Malley* court found that the NASD rule did not preempt the state-law claim, reasoning that the rule did not "purport to create a 'safe harbor'" for brokers and that "additional disclosure requirements concerning the broker's self-interest would be the same for all customers, [and so] would not be unduly burdensome or otherwise interfere with the purpose of the rule." *Id.* at 849. This reasoning cannot be squared with the Nevada Supreme Court's holding that petitioners' claims are preempted.

The NASD rule in *O'Malley*, like respondents' rules in this case, is a rule of a self-regulatory organization designed to promote the efficient operation of the national securities markets. Like the plaintiffs in *O'Malley*, petitioners claim that respondents have affirmatively misrepresented, and have failed to disclose material facts about, their operation of the stock borrow program. Nothing in the rules on which the court below relied creates a "safe harbor" from such claims. Moreover, respondents could have protected themselves from any such claims with simple,

general disclosures about the risks of phantom shares created by the stock borrow program, and doing so would not have interfered with any legitimate operation of that program. Accordingly, the courts of Delaware would have granted relief to petitioners on the basis of a disagreement with the courts of Nevada about a dispositive question of federal law.

A similar case from the California Supreme Court, *Diamond Multimedia Systems, Inc. v. Superior Court*, 968 P.2d 539 (Cal. 1999), strongly suggests that California would agree with Delaware. *See id.* at 545 (stating that, in market manipulation actions, "[s]hareholders' rights under state and federal law are cumulative," and "Congress has confirmed the independent force of state securities law").

By contrast, the highest courts of New York and Pennsylvania have addressed closely related questions and adopted a position that aligns with that of Nevada. In *Guice v. Charles Schwab & Co.*, 674 N.E.2d 282 (N.Y. 1996), the New York Court of Appeals held that state-law claims based on a broker-dealer's failure to make timely and detailed disclosure of "order flow payments"[18] were preempted by an SEC regulation that had imposed looser disclosure requirements. *See id.* at 289-90. The court held that the effect of tighter state-by-state disclosure requirements would lead to a "'chaotic regulatory structure'" that Congress could not have intended. *Id.* at 290 (quoting *International Paper Co. v. Ouellette*, 479 U.S. 481, 497 (1987)); *see Shulick v. PaineWebber, Inc.*, 722 A.2d 148, 151 (Pa. 1998) (following *Guice*); *see also Dahl v. Charles Schwab &*

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[18] These are payments for routing customers' orders to other dealers for execution. *See Guice*, 674 N.E.2d at 284.

Co., 545 N.W.2d 918, 925 (Minn. 1996) (reaching a similar conclusion with regard to consent requirements under Minnesota agency law). These cases demonstrate the well-entrenched conflict among state courts of last resort on how preemption affects state-law securities claims.[19]

2. Review of the Nevada Supreme Court's judgment also is warranted because that decision implicates a broader division of the state and federal courts over when a federal regulatory approval conflicts with (and so preempts) state-law claims for misrepresentations about the action approved.

The better and more widely accepted view is that state-law claims for fraud, or other claims based on false or misleading representations, rarely conflict with the federal purpose for authorizing regulated activity, because federal policy will almost always be furthered by preventing fraud. The California Supreme Court, for example, has held that federal approval of a wine bottler's label does not preempt a state statute that prohibited the label as misleading because the label contained the word "Napa" but the wine was not made from Napa grapes. *See Bronco Wine Co. v. Jolly*, 95 P.3d 422, 424-25 (Cal. 2004). In reaching that conclusion, the court reasoned that "Congress's overall purposes . . . have been to support the states' efforts to protect consumers from

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[19] In *O'Malley*, the Delaware court distinguished *Guice* because the New York court had relied on a "regulatory history" in which "the SEC had . . . rejected as unworkable" the "very order flow payment disclosures" that the "*Guice* plaintiffs were claiming that state law required." 742 A.2d at 849. No such history is present in this case. If the distinction drawn in *O'Malley* is correct, it shows merely that New York might agree with Delaware rather than Nevada on the question presented, and does not resolve the conflict between this case and *O'Malley*.

misleading labeling, not to permit [such] labeling." *Id.* at 457. The Second Circuit has likewise held that federal regulations governing the drug testing of airline employees did not preempt state-law claims based on misrepresentations made in relation to the tests because those regulations did not contain any provisions regarding false statements. *See Drake v. Laboratory Corp. of Am. Holdings*, 458 F.3d 48, 65-66 (2d Cir. 2006).[20]

Other courts, however, have taken a more aggressive view of preemption that has substantially restricted the scope of state laws providing remedies for misrepresentation. The decision below is one such example, and a recent decision of the Third Circuit provides another. In *Pennsylvania Employees Benefit Trust Fund v. Zeneca Inc.*, 499 F.3d 239 (3d Cir. 2007), *petition for cert. pending*, No. 07-822 (filed Dec. 18, 2007), the Third Circuit held that Food and Drug Administration ("FDA") approval of a label for a prescription drug conflicted with and so preempted state-law claims that a drug manufacturer's advertis-

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[20] In addition, in a decision that sharply conflicts with the decision below, a New Mexico intermediate court of appeals held that state-law fraud claims could proceed against a health-care provider based on a letter containing false statements, even though the text of the letter had been approved by the Health Care Financing Administration. *See Palmer v. St. Joseph Healthcare P.S.O., Inc.*, 77 P.3d 560, 572-75 (N.M. Ct. App. 2003) (reasoning that "Congress could not have intended to grant a federal agency the prerogative" to authorize false statements while leaving the victims "no recourse in court"), *cert. dismissed*, 101 P.3d 808 (N.M. 2004) (table). *See also True v. American Honda Motor Co.*, 520 F. Supp. 2d 1175, 1180-81 (C.D. Cal. 2007) (finding that Environmental Protection Agency ("EPA") approval of a fuel efficiency label did not preempt state-law fraud claims based on advertising other than the label itself).

ing was fraudulent or misleading because it falsely claimed the drug was superior over a competing product. *See id.* at 250-52. A strong dissent in *Pennsylvania Employees* correctly pointed out that the FDA had "not approved the veracity of the particular advertisements in question, and . . . [the] plaintiffs [were] not attacking, directly or indirectly, the labeling approved by the FDA." *Id.* at 255 (Cowen, J., dissenting). The majority, however, opined that "[t]he high level of specificity in federal law and regulations with respect to prescription drug advertising" alone was sufficient to establish conflict preemption. *Id.* at 252. Indeed, in denying leave to amend, the *Pennsylvania Employees* court further held that it would not matter even if the FDA had explicitly refused to approve the specific advertising claims made or if the drug manufacturer had represented to the FDA that it would not make them. *See id.* at 252-53.

These varied decisions show wide-ranging disagreement about the appropriate treatment of state-law misrepresentation claims, and the decision of the Nevada Supreme Court in this case deepens that existing division of authority. For example, *Bronco Wine* requires a showing, before a state law prohibiting fraud and misleading statements will be found to conflict with a federal regulatory authorization, that the authorization approved the particular statements at issue. *See* 95 P.3d at 454 (rejecting an argument that federal law "*authorize[d]*" the misleading statement on the label and stating instead that federal law merely "*d[id] not prohibit*" it). Applied to this case, that reasoning would require reversal, because the NSCC regulations approved by the SEC did not authorize the false and misleading

statements for which petitioners seek relief. By contrast, *Pennsylvania Employees* requires no such showing, as the Nevada Supreme Court did not in this case. Similarly, the Second Circuit's decision in *Drake* requires that the federal authorization from which preemption is to be derived at least have something to do with the regulation of false statements – a requirement that, however basic it may seem, the Nevada Supreme Court did not observe here. The applicable standards are unclear, and a grant of review will enable this Court to bring needed clarity to this area of the law.

B. The Decision Below Conflicts With *Bates*

The decision of the Nevada Supreme Court is, moreover, incorrect and in conflict with several prior decisions of this Court, and that conflict also warrants review. Its clearest error is its failure to follow the reasoning of *Bates*. In that case, this Court interpreted an express preemption clause in the Federal Insecticide, Fungicide, and Rodenticide Act ("FIFRA"), which provided that the States "'shall not impose or continue in effect any requirements for labeling or packaging in addition to or different from those required under [FIFRA].'" 544 U.S. at 436 (quoting 7 U.S.C. § 136v(b)). Reading that clause, the Court reasoned that it would not preempt a state law that was "equivalent to, and fully consistent with, FIFRA's misbranding provisions." *Id.* at 447. Although the preemption arguments in *Bates* concerned an express preemption clause, the Court's reasoning replicated the classic conflict preemption inquiry when it concluded that "[p]rivate remedies that enforce federal misbranding requirements would

seem to aid, rather than hinder, the functioning of FIFRA." *Id.* at 451.[21]

Further, the *Bates* Court was unpersuaded by the argument that FIFRA's national purpose of uniformity would be impeded by subjecting pesticide manufacturers to the verdicts of different juries in different States – provided that the juries were applying state-law standards that were "fully consistent with federal requirements." *Id.* at 451-52. The Court emphasized the "basic presumption against pre-emption" of state-law causes of action and the broad role for state regulation under FIFRA. *Id.* at 449. And it reasoned that Congress would have "expressed [its] intent more clearly" than it had in § 136v(b) if it "had intended to deprive injured parties of a long available form of compensation." *Id.* at 449-50 (citing *Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 251 (1984)); *see Silkwood*, 464 U.S. at 251 (finding it "difficult to believe that Congress would, without comment, remove all means of judicial recourse for those injured by illegal conduct").

The Nevada Supreme Court's reasoning contravenes *Bates* in several respects. The state supreme court should have considered, as *Bates* did, whether the state-law remedies sought by petitioners would "aid, rather than hinder," 544 U.S. at 451, the purposes of the federal securities laws. To do so, the

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[21] *See Hines*, 312 U.S. at 67 (holding that conflict preemption applies when a state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress"); *cf. Metrophones Telecomms., Inc. v. Global Crossing Telecomms., Inc.*, 423 F.3d 1056, 1073 (9th Cir. 2005) (interpretation of express preemption clause precluding "inconsistent" state-law claims is "substantially identical to the analysis of implied conflict preemption"), *aff'd*, 127 S. Ct. 1513 (2007).

court would have needed to take account of the "fundamental purpose" of the 1934 Act to implement a "philosophy of full disclosure," *Basic Inc. v. Levinson*, 485 U.S. 224, 230 (1988) (internal quotation marks omitted), and to give "due regard" for "the protection of investors," § 78q-1(a)(2)(A). In this respect, the state supreme court's conclusion that petitioners' damages "constitute an exploitable flaw inherent in the federally authorized system" misunderstands the correct interplay between federal and state law. If petitioners have a remedy for respondents' fraudulent statements and omissions, then investors can be protected from the consequences of any flaw with tools that Congress contemplated would be available for such purposes – state-law remedies.[22]

Similarly, the court below erred by failing to give adequate weight to Congress's decision to preserve, when it enacted the 1934 Act, "any and all other rights and remedies that may exist at law or in equity." § 78bb(a); *see Leroy v. Great Western United Corp.*, 443 U.S. 173, 182 n.13 (1979) (recounting a draftsman's statement that the "purpose of [§ 78bb(a)] was to leave the States with as much leeway to regulate securities transactions as the Supremacy Clause would allow them in the absence of such a provision"). This savings clause reflects Congress's

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[22] If correct, the decision below also would imply that petitioners have no remedy available under the SEC's Rule 10b-5 – because their state-law claims include a state statute similar to that rule. *See* Nev. Rev. Stat. § 90.570. But it is absurd to say that the SEC either did, or could, authorize respondents to make false and misleading statements in violation of federal law. The logical implication of this result from the premises adopted by the Nevada Supreme Court is merely another sign of that court's error.

intent to preserve state jurisdiction to an even greater extent than does the language in FIFRA, interpreted by *Bates*. Yet the Nevada Supreme Court's analysis gave far less weight to the purposes of the state law, and to the harmony between the purposes of federal and state law, than this Court did in *Bates*. It also neglected this Court's warning that claims about the "disruptive effects" of state-law remedies may be "exaggerate[d]," and this Court's reliance on the "long history of [state] tort litigation" in the relevant field, *Bates*, 544 U.S. at 449, 451, instead simply assuming that state law would be diverse and so disrupt federal policy.[23] This analytic leap is contrary not only to *Bates*, but also to *Cipollone v. Liggett Group, Inc.*, 505 U.S. 504 (1992), in which a plurality of this Court explained that "[s]tate-law prohibitions on false statements of material fact do not create 'diverse, nonuniform, and confusing' standards," but instead "rely only on a

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[23] Indeed, the court's reasoning on the disruption it feared is difficult to follow. It states that "[i]mposing any state law requirement for efficiency, which, in the absence of any federal standard, would be necessary before appellants could show that respondents have failed to efficiently clear and settle securities transactions here, would compel respondents to alter their federally approved manner of operating the Stock Borrow Program." Pet. App. 20a. But all that is necessary here is to require respondents to disclose and not conceal the fact that their practices have injected phantom shares into the market that dilute the value of validly issued shares. The lower court's holding flies in the face of the federal securities laws' dedication to investor protection, and also of the long-standing requirement that federal preemptive intent be "clear and manifest." *Bates*, 544 U.S. at 449 (quoting *New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 514 U.S. 645, 655 (1995) (quoting, in turn, *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947))) (internal quotation marks omitted)).

single, uniform standard: falsity." *Id.* at 529.[24] The Nevada Supreme Court dissenters likewise found, correctly, that state-law claims based on misrepresentation in no way interfere with the federal regime because they merely hold respondents to the centuries-old prohibition against misrepresentation. *See supra* pp. 17-18.

Finally, the state supreme court neglected *Bates*'s teaching that federal approval of a regulated activity confers no automatic imprimatur on representations made in connection with that activity, especially when those representations themselves are not approved by the federal agency. *See* 544 U.S. at 443-45. Just as the EPA's approval of the pesticide label at issue in *Bates* did not prevent the plaintiffs in that case from arguing that the manufacturers had breached the warranty claims in those labels (or oral representations not on the labels), *see id.* at 444 & n.17, so the SEC's approval of respondents' regulations creating the stock borrow program should not preempt petitioners' state-law claims seeking relief for respondents' misrepresentations about that program.

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[24] The plurality opinion in *Cipollone* was, in its reasoning on this point, the "narrowest ground[]" for the Court's judgment, and should therefore have been treated by the court below as controlling. *Marks v. United States*, 430 U.S. 188, 193 (1977) (internal quotation marks omitted); *see Cipollone*, 505 U.S. at 544 (Blackmun, J., concurring in part, concurring in the judgment in part, and dissenting in part) (adopting the broader theory that the statute at issue preempted no common-law claims whatsoever).

C. The Petition Raises An Important Issue Meriting This Court's Review

The scope of preemption in this context implicates the federal and state policies of full and fair disclosure to investors in the securities markets and the remedies available to investors in all 50 States. The Nevada Supreme Court's decision rests on a theory that, even though petitioners have been damaged by respondents' conduct, federal policy precludes any State from providing a remedy for the damage respondents have caused.

If the state court were correct, federal policy would bar state remedies that serve the primary goal of the federal securities laws themselves. But that perverse reasoning is inconsistent with the express statutory language and decades of precedent. If the state supreme court's judgment is allowed to stand, petitioners, and many other investors in a similar predicament, will be deprived of an important tool for vindicating the protections accorded them under federal and state law. Moreover, the state courts' erroneous overreading of federal preemption law may infect other cases that turn on this important set of questions about the interaction of federal and state authority.

In addition, this case presents a good vehicle for this Court to clarify the law. The holding of the Nevada Supreme Court rested solely on federal law and disposed of all of petitioners' claims, leaving no room for further proceedings. *See* Pet. App. 24a. In addition, that court, while erring fundamentally in its conflict-preemption analysis, correctly held that field preemption does not apply in this case, thus narrowing the issues to the key points in contention. *See id.* at 14a-15a. If this Court grants review, there

will be no impediment to it resolving the important question presented.

II. IN THE ALTERNATIVE, THIS CASE SHOULD BE HELD PENDING THIS COURT'S DECISION IN *ALTRIA*.

Although this case is fully appropriate for this Court's plenary review, it also is possible that the relevant law may be sufficiently clarified by this Court's forthcoming decision in a recently granted case. On January 18, 2008, this Court granted review in *Altria Group, Inc. v. Good*, No. 07-562. Among the questions presented in *Altria* is whether the FDA's alleged authorization of certain statements by cigarette manufacturers about the nicotine and tar content of their cigarettes conflicts with, and so implicitly preempts, state-law claims that the statements in question are false or misleading. *See Altria* Pet. i.

If this Court reaches the merits of the implied conflict-preemption claim in *Altria*, its decision will likely shed light on the contested questions discussed *supra*, pp. 20-26, especially the appropriate analysis of conflict preemption when state law provides a remedy for misrepresentations made in connection with federally authorized activity. Were that to occur, the Court's normal practice of granting, vacating, and remanding would be appropriate to permit the Nevada Supreme Court to reconsider its holding on implied conflict preemption in light of this Court's most recent pronouncement and application of those principles. This case would nevertheless be a more secure vehicle for resolving and applying implied conflict-preemption principles, because it is possible that the Court will decide *Altria* purely on express preemption grounds and because the implied conflict-

preemption claim in *Altria* may be resolved on the ground that, because the FDA did not formalize its authorization in a rule, the authorization had no preemptive effect. *See Altria* Pet. 22-24.

Nevertheless, if this Court chooses not to grant plenary review in this case at this time, there is a significant possibility that its decision in *Altria* will make clear whether the decision below is on a secure footing. Accordingly, as an alternative to a grant of certiorari, this Court should hold this case for appropriate disposition in light of *Altria*.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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SUPREME COURT OF NEVADA

No. 45364

NANOPIERCE TECHNOLOGIES, INC., ET AL.,
Appellants,

v.

THE DEPOSITORY TRUST AND CLEARING CORPORATION, ET AL.,
Respondents.

September 20, 2007

BEFORE THE COURT EN BANC.

By the court, SAITTA, J.:

This case arises from respondents' use of the Stock Borrow Program to facilitate clearing and settling certain broker-to-broker securities transactions. "Clearing and settling" essentially refers to the process by which record ownership of securities is exchanged for funds when sellers transfer securities to purchasers. Respondents are a holding company and its two subsidiary clearing agencies. The clearing agencies and the Stock Borrow Program were created under federal Securities Exchange Commission (Commission) guidelines to expedite the clearing and settling process that, when performed on the scale that respondents perform it – millions of transactions daily – would otherwise be cumbersome, confusing, and costly.

According to appellants Nanopierce Technologies, Inc., and some of its shareholders, respondents' use of the Stock Borrow Program impermissibly decreased Nanopierce's stock value, irrespective of normal market forces. Consequently, appellants instituted the case below, asserting state law challenges to respondents' operation, and representation to participants, of the Stock Borrow Program. The district court ultimately dismissed the action, concluding that federal law in the area of clearing and settling securities transactions preempted appellants' claims. This appeal followed.[1]

The question presented is whether section 17A of the Securities Exchange Act of 1934 preempts appellants' state law claims for damages. We agree with the district court that appellants' state law challenges related to the Stock Borrow Program are preempted by federal statutes and regulations. Specifically, we conclude that, because the state law on which appellants base their claims poses an obstacle to respondents' accomplishment of congressional objectives as explicitly stated in and gleaned from the Securities Exchange Act's framework, and because respondents' compliance with both state and federal requirements concerning the securities transactions at issue in this case is impossible, section 17A of the Securities Exchange Act preempts appellants' claims.

In explaining that determination, we initially set forth a somewhat detailed discussion of respondents'

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[1] Respondents have filed a motion under NRAP 31(d) requesting leave to file a "Statement of Supplemental Authorities." Having considered the motion, and appellants' opposition thereto, we grant it. Accordingly, we direct the court clerk to file respondents' "Statement of Supplemental Authorities," provisionally received on June 22, 2007.

and the Stock Borrow Program's federally enacted roles in clearing and settling broker-to-broker securities transactions, as necessary to understand appellants' causes of action. We then generally set forth the various preemption analyses, before determining the preemption analytical framework necessary to address appellants' causes of action. Finally, we analyze appellants' causes of action in light of that framework to determine whether federal enactments with respect to clearing and settling securities transactions preempt appellants' state law causes of action.

The Stock Borrow Program and its primary clearing agencies – The Depository Trust Company and The National Securities Clearing Corporation

The Stock Borrow Program is principally a result of difficulties that arose under the Securities Exchange Act of 1934, which Congress enacted generally to regulate and control securities transactions in interstate commerce, and specifically to "remove impediments to and perfect the mechanisms of a national market system for securities and a national system for the clearance and settlement of securities transactions."[2] In 1975, to modernize the system in light of technical advances, Congress amended the Securities Exchange Act of 1934 to add section 17A, which directed the Commission to establish a national system "to facilitate" the efficient clearance and settlement of securities transactions, including registering and regulating clearing agencies.[3]

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[2] 15 U.S.C. § 78b (2000).

[3] *Id.* § 78q-1(a)(2)(A).

The primary clearing agencies that the Commission registered, under section 17A, are respondents The Depository Trust Company (DTC) and The National Securities Clearing Corporation (NSCC),[4] subsidiaries of respondent The Depository Trust and Clearing Corporation. With respect to registering the NSCC, the Commission specifically determined that the NSCC's "by-laws, rules, procedures, and systems," including the Stock Borrow Program, were consistent with the Commission's standards and requirements.[5] The DTC and the NSCC are also registered with the Commission as self-regulatory organizations; the Commission has effectively delegated some of its authority to regulate the clearance and settlement of securities transactions to respondents.[6] Respondents thus stand in the Commission's shoes when performing their functions.[7]

Together, the DTC and NSCC, as regulated by the Commission, provide automated clearance and settlement of broker-to-broker securities transactions.[8]

The DTC

The DTC, for its part in facilitating the clearance and settlement of securities transactions, acts as a stock depository, retaining in its vaults the physical

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[4] *See* Depository Trust Co., et al., 48 Fed.Reg. 45,167 (SEC Oct. 3, 1983).

[5] *See id.* at 45,178; *see also* 15 U.S.C. § 78q-1(b)(2)-(3); National Securities Clearing Corporation, 46 Fed.Reg. 3104 (proposed Jan. 13, 1981).

[6] *See* 15 U.S.C. § 78s(a) (2000); Self-Regulatory Organizations, Exchange Act Release No. 34-47978, 80 SEC Docket 1143 n. 50 (June 4, 2003).

[7] *See Dexter v. Depository Trust and Clearing Corp.*, 406 F.Supp.2d 260, 263 (S.D.N.Y.2005).

[8] *See* 15 U.S.C. § 78q-1(b)(3)(A).

stock certificates that a broker has deposited with it on behalf of an investor. Any broker deposit is reflected as a credit in that broker's corresponding DTC account. Although brokers deposit the physical stock certificates with the DTC on behalf of individual investors, all certificates are held in the DTC's vaults in the name of the DTC's nominee, Cede & Co. Thus, once deposited, stock certificate ownership changes are merely recorded electronically in the brokers' respective DTC accounts – no movement of the physical stock certificates occurs.

The NSCC

While the DTC's role in clearing and settling securities transactions essentially includes only retaining the physical stock certificates and updating brokers' DTC accounts to reflect transfers of stock ownership, the NSCC facilitates the actual clearance and settlement of the securities by (1) acting as an intermediary between brokers engaged in a securities transaction, and (2) tracking, over a designated trading period, a broker's transactions with respect to a specific security.

In its role as an intermediary, the NSCC assumes the payment and delivery obligations of the buying and selling brokers, respectively. As regards the NSCC's tracking function, the NSCC keeps track of all of a broker's transactions with respect to a specific security over a designated trading period. This function allows a broker to deliver to or receive from the NSCC, which as noted has assumed the broker's purchase and delivery obligations, the net amount resulting from his purchase and sales of that particular security at the end of the designated trading period.

After the NSCC calculates a broker's payment or delivery obligation with respect to a specified security for a designated trading period, the broker normally owes or is owed shares of that security. The NSCC then transmits that information to the DTC for processing. For the selling broker, the DTC compares the broker's share delivery obligation, if any, to the amount of that share held in the broker's DTC account, to determine whether the broker possesses enough shares to fulfill his delivery obligation. If enough shares are present in the selling broker's DTC account to fulfill that delivery obligation, delivery of those shares occurs by sending the shares through the NSCC to the DTC account of the party owed the securities, the buying broker. If, however, the selling broker does not have enough shares in his DTC account to cover the obligation, *i.e.*, the broker has sold more shares than he possesses, two options for covering the unfilled obligation generally exist: (1) the buying broker, who is owed the shares, after notifying the NSCC, may purchase in the open market the number of shares owed to him – so-called buying-in; or (2) the buying broker simply can wait for the amount of shares owed to him to become available as other securities transactions are processed through the NSCC. According to appellants, these two options were available to a broker before the NSCC implemented the Stock Borrow Program.

Stock Borrow Program

Apparently to obviate the need for a buying broker to exercise either of the two aforementioned options, *i.e.*, to reduce the instances of a buying broker failing to receive the shares owed to him, the NSCC implemented the Stock Borrow Program. The Stock Borrow Program enables NSCC and DTC brokers to lend

shares from their DTC accounts to cover another broker's failure to deliver shares to the NSCC, before any actual failure to deliver occurs. The Stock Borrow Program essentially operates by allowing brokers, otherwise unrelated to the securities transaction that resulted in the delivery obligation, to loan securities that they have on deposit with the DTC to satisfy the delivery obligation.

According to appellants, respondents, as well as brokers, are able to profitably manipulate the Stock Borrow Program, to appellants' detriment. Appellants contend that respondents use undisclosed internal loopholes in the Stock Borrow Program for their own benefit by generating so-called phantom shares, which, appellants allege, have a dilutive effect on Nanopierce's stock value. Because respondents purportedly obscure this process and its effects, appellants assert that they are entitled to relief under state law.

Preemption

Having set forth respondents' operation of the Stock Borrow Program and the bases of appellants' challenges, we now discuss whether federal law preempts appellants' state law challenges related to the Stock Borrow Program. Whether state law is preempted by a federal statute or regulation is a question of law,[9] subject to our de novo review.[10] As an initial matter, we note that, although the Stock Borrow Program itself and the rules describing and

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[9] *Kinkel v. Cingular Wireless LLC*, 857 N.E.2d 250, 260 (Ill. 2006); *Doty v. Frontier Communications Inc.*, 36 P.3d 250, 257 (Kan.2001).

[10] *SIIS v. United Exposition Services Co.*, 109 Nev. 28, 30, 846 P.2d 294, 295 (1993).

governing its operation are not federal law *per se*, the Commission promulgated federal regulations, based on Congress's directive set forth by statute, section 17A of the Securities Exchange Act of 1934, as amended,[11] that, among other things, approved the NSCC's rules concerning the Stock Borrow Program's operation.[12]

The preemption doctrine, which provides that federal law supersedes conflicting state law, arises from the Supremacy Clause of the United States Constitution.[13] The Supremacy Clause, found in Article VI, requires that "the Laws of the United States . . . shall be the supreme Law of the Land; . . . any Thing in the Constitution or Laws of any State to the Contrary notwithstanding."[14] Thus, when a conflict exists between federal and state law, valid federal law overrides, *i.e.*, preempts, an otherwise valid state law.[15] Whether a federal enactment preempts state law is fundamentally a question of congressional intent – did Congress expressly or impliedly intend to preempt state law?[16] Even when implied, Congress's

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[11] 15 U.S.C. § 78q-1(a)(2)(A).

[12] *See* National Securities Clearing Corporation, 46 Fed.Reg. 3104 (proposed Jan. 13, 1981); Depository Trust Co., et al., 48 Fed.Reg. 45,167 (SEC Oct. 3, 1983); *see also Hillsborough County v. Automated Medical Labs.*, 471 U.S. 707, 713 (1985) (noting that "state laws can be pre-empted by federal regulations as well as by federal statutes").

[13] *Crosby v. National Foreign Trade Council*, 530 U.S. 363, 372 (2000) (stating that "[a] fundamental principle of the Constitution is that Congress has the power to preempt state law").

[14] U.S. Const. art. VI, cl. 2.

[15] *Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 516 (1992).

[16] *Id.*; *see also Barnett Bank of Marion Cty., N.A. v. Nelson*, 517 U.S. 25, 30 (1996).

intent to preempt state law, in light of a strong presumption that areas historically regulated by the states generally are not superseded by a subsequent federal law, must be "'clear and manifest.'"[17]

Express preemption

Congress expressly preempts state law when it explicitly states that intent in a statute's language.[18] Thus, when determining whether Congress has expressly preempted state law, a court must examine statutory language – any explicit preemption language generally governs the extent of preemption.[19]

Implied preemption

When Congress does not include statutory language expressly preempting state law, Congress's intent to preempt state law nonetheless may be implied in two circumstances known as field preemption and conflict preemption. First, under field preemption, preemption is implied when congressional enactments so thoroughly occupy a legislative field, or touch a field in which the federal interest is so dominant, that Congress effectively leaves no room for states to regulate conduct in that field.[20] To determine whether Congress has preempted a field of law, the entire regulatory scheme must be examined to determine whether, based on its level of compre-

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[17] *Bates v. Dow Agrosciences LLC*, 544 U.S. 431, 449 (2005) (quoting *New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 514 U.S. 645, 655 (1995)); *see also Davidson v. Velsicol Chemical*, 108 Nev. 591, 594, 834 P.2d 931, 933 (1992).

[18] *Cipollone*, 505 U.S. at 516.

[19] *Id.* at 517; *Davidson*, 108 Nev. at 594, 834 P.2d at 932.

[20] *Cipollone*, 505 U.S. at 516; *Hillsborough County*, 471 U.S. at 713.

hensiveness or the nature of the field regulated, Congress intended to preclude states from also imposing requirements on that field.[21] If, based on that examination, it can be inferred that Congress intended to occupy that legislative field, state requirements are preempted regardless of any specific law's conflict.[22]

Second, even when Congress's enactments do not pervade a legislative field or regulate an area of uniquely federal interest, Congress's intent to preempt state law is implied to the extent that federal law actually conflicts with any state law.[23] Conflict preemption analysis examines the federal statute as a whole to determine whether a party's compliance with both federal and state requirements is impossible or whether, in light of the federal statute's purpose and intended effects, state law poses an obstacle to the accomplishment of Congress's objectives.[24]

Field preemption

As an initial matter, we note that, although the parties do not address whether appellants' claims are expressly preempted by any explicit statutory language, no provision within the Securities Exchange Act of 1934, or Congress's amendments thereto, reveals congressional intent to do so.[25] On appeal,

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[21] *Hillsborough County*, 471 U.S. at 713.

[22] *Cipollone*, 505 U.S. at 516.

[23] *Id.*

[24] *Crosby*, 530 U.S. at 373.

[25] We note, moreover, that although an express preemption provision raises a reasonable inference that it evidences the entire extent of Congress's intent to preempt, so that further analysis to determine if any other matters are preempted under an implied preemption theory is unnecessary, that inference is merely an indication of congressional intent, and thus does

appellants essentially contend that the district court erred in applying a field preemption analysis to their claims and concluding in light of that analysis that, because Congress's enactments so thoroughly occupy the legislative field of clearing and settling securities transactions, Congress intended to preclude state law claims like appellants' from imposing any additional requirements on that field. Implicit in appellants' argument is that conflict preemption is the appropriate analytical framework with respect to determining whether federal law governing clearing and settling securities transactions conflicts with and thus preempts their state law claims. According to appellants, their state law claims do not actually conflict with Congress's statutory framework.[26]

With regard to whether Congress intended to occupy the entire field of securities regulation, or more narrowly, the field of clearing and settling securities transactions, provisions within the statutory framework, analyzed in light of states' historical domination over the field of securities regulation, indicate that Congress did not intend to occupy those fields to the exclusion of state law. Although the statutory scheme indicates Congress's intent to occupy much of the securities regulation area, including the clearing and settling of securities transac-

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not foreclose the possibility of implied preemption. *Freightliner Corp. v. Myrick*, 514 U.S. 280, 288-89 (1995) (citing *Cipollone*, 505 U.S. at 518).

[26] Appellants' arguments notwithstanding, the district court's order dismissing appellants' complaint did not expressly state whether the order was based on field or conflict preemption, though the court analyzed and employed language characteristic of both doctrines. The court mentioned express preemption only prefatorily.

tions, an examination of Congress's statutory scheme with respect to securities transactions does not reveal the comprehensiveness necessary to infer that Congress intended to wholly occupy that legislative field.[27]

Specifically, when enacting the Securities Exchange Act of 1934, Congress included a provision recognizing that the Securities Exchange Act did not impact any non-conflicting state securities laws:

> [T]he rights and remedies provided by [the Securities Exchange Act of 1934] shall be in addition to any and all other rights and remedies that may exist at law or in equity. . . . [N]othing in this [Act] shall affect the jurisdiction of the securities commission . . . of any State over any security or any person insofar as it does not conflict with the provisions of this [Act] or the rules and regulations thereunder.[28]

This provision does not indicate congressional intent to occupy the entire field of securities regulation, but rather, to occupy that field only inasmuch as state laws "conflict with the provisions of [the Act] or the rules and regulations thereunder."[29]

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[27] *See Baker, Watts & Co. v. Miles & Stockbridge*, 876 F.2d 1101, 1107 (4th Cir.1989) (recognizing that, within the field of securities, "[t]he states enjoy broad powers to regulate such diverse subjects as [the following]: the registration of securities; the registration of broker-dealers, agents, and investment advisors; and fraud in the sale or purchase of securities and the rendering of investment advisory services").

[28] 15 U.S.C. § 78bb(a).

[29] *Id.*; *accord Herman & MacLean v. Huddleston*, 459 U.S. 375, 383 (1983) (noting that 15 U.S.C. § 78bb(a) revealed that

Likewise, with respect to the narrower field of a uniform nationalized system for clearing and settling securities transactions, as mentioned, Congress authorized the Commission to regulate this area in 1975 when it amended the Securities Exchange Act of 1934 to add section 17A.[30] Although no court opinion appears to address Congress's preemptive intent with respect to section 17A, a provision within section 17A and a subsequent amendment indicate an intent to not wholly occupy that legislative field.

For instance, Congress included a provision in section 17A stating that section 17A shall not "be construed to impair the authority of any State banking authority or other State . . . regulatory authority having jurisdiction over a person registered as a clearing agency . . . to make and enforce rules . . . which are not inconsistent with" section 17A and any rules and regulations promulgated based on section 17A.[31] That provision unambiguously signifies that Congress did not intend to occupy the entire field of national clearance and settlement of securities transactions, since Congress explicitly left room for state banking and regulatory authorities to supplement that legislative field's regulation, so long as any state regulation is not inconsistent with section 17A.

A subsequent amendment likewise reveals congressional intent not to comprehensively regulate the entire national securities clearance and settlement field. Congress amended section 17A, in 1990, to add the following provisions allowing the Commission to

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Congress "rejected the notion that the express remedies of the securities laws would pre-empt all other rights of action").

[30] 15 U.S.C. § 78q-1(a)(2)(A).

[31] 15 U.S.C. § 78q-1(d)(4).

adopt rules inconsistent with state law, but permitting, within two years' time, the states to then enact laws that contradict the Commission's rules:

> Notwithstanding any provision of State law, . . . [after making certain findings,] the [Securities Exchange] Commission may adopt rules concerning . . . the transfer of certificated or uncertificated securities . . . or limited interests (including security interests) therein; and . . . [the] rights and obligations of purchasers, sellers, owners, lenders, borrowers, and financial intermediaries (including . . . clearing agencies) involved in or affected by such transfers, and the rights of third parties whose interests in such securities devolve from such transfers.[32]
>
> Any State may, prior to the expiration of 2 years after the [Securities Exchange] Commission adopts a rule under this subsection, enact a statute that specifically refers to this subsection and the specific rule thereunder and establishes, prospectively from the date of enactment of the State statute, a provision that differs from that applicable under the [Securities Exchange] Commission's rule.[33]

In light of these two provisions, Congress explicitly left room for state laws to supplement the federal regulatory scheme and thus did not reveal a "'clear and manifest'" intent to occupy the field of regulating

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[32] 15 U.S.C. § 78q-1(f)(1).

[33] 15 U.S.C. § 78q-4(f)(3).

clearing agencies.[34] Accordingly, no field preemption exists.[35]

Conflict preemption

Because Congress did not expressly preempt appellants' claims by explicitly stating that intent within the provisions of the Securities Exchange Act, or its amendments thereto, and no field preemption exists, conflict preemption analysis is the appropriate analytical framework in this matter. As noted, conflict preemption analysis generally requires measuring state law claims against the federal statutory framework, and the federal statute's effects and purpose as revealed by that framework, to determine whether a party's compliance with both state and federal law requirements is impossible, or whether the act's purpose would be frustrated if state law were to apply. Here, then, we must determine whether imposing the requirements implicated by appellants' state law claims on respondents is inconsistent with section 17A's purpose of allowing the Commission to regulate and control a national system for clearing and settling securities transactions.[36]

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[34] *Bates*, 544 U.S. at 449 (quoting *New York State Conference of Blue Cross & Blue Shield Plans*, 514 U.S. at 655).

[35] Importantly, moreover, the question here, whether appellants' state-law based claims fit within any of section 17A's provisions to the extent that those provisions leave room for states to impose their own requirements is somewhat inapposite to the issue whether, in light of the statutory scheme Congress enacted, did it manifest a clear intention to pervade the entire field of regulating clearing agencies so that any state law claims would be preempted. In light of the discussed provisions, Congress did not clearly manifest that intent.

[36] *See* 15 U.S.C. § 78q-1(a)(2)(A) and (B) (directing the Commission to "facilitate the establishment of a national system for the prompt and accurate clearance and settlement" of secu-

Appellants' misrepresentation-based claims

To determine whether appellants' claims are inconsistent with respondents' authority delegated from the Commission to operate a Commission-approved national system of clearance and settlement of securities transactions, we necessarily examine the claims.[37] For the purposes of this examination, appellants' claims can be divided into two groups: (1) misrepresentation claims, and (2) non-misrepresentation claims.

Appellants' complaint asserted four misrepresentations with respect to respondents' operation of the Stock Borrow Program. Each alleged misrepresentation provides the basis for appellants' separately asserted causes of action for negligent misrepresentation, intentional misrepresentation, fraudulent misrepresentation, and securities fraud under NRS 90.570. Regardless of the state of mind necessary, if any, to determine liability under appellants' various misrepresentation-based causes of action,[38] the

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rities transactions, including registering and regulating clearing agencies).

[37] *Cf. Cipollone*, 505 U.S. at 524-30 (engaging in a claim-by-claim analysis to determine any express federal preemption of the state law causes of action in that case).

[38] *See Secretary of State v. Tretiak*, 117 Nev. 299, 22 P.3d 1134 (2001) (providing that scienter is not a required element of a cause of action under NRS 90.570 for securities fraud); *Barmettler v. Reno Air, Inc.*, 114 Nev. 441, 956 P.2d 1382 (1998) (noting that one liable for negligent misrepresentation must have failed to exercise reasonable care with regard to the information communicated and that one liable for fraudulent misrepresentation generally must have communicated information knowing its falsity); *Collins v. Burns*, 103 Nev. 394, 741 P.2d 819 (1987) (noting that one liable for intentional (or fraudulent) misrepresentation generally must have communicated information knowing its falsity).

essence of any misrepresentation claim is a false or misleading statement that harmed appellants.[39] Moreover, in addressing appellants' misrepresentation claims in the context of this appeal from a district court order dismissing their complaint, this court assumes appellants' allegations are true[40] – *i.e.*, that respondents made the purported misrepresentations.

Appellants contend that the NSCC, in its rules and procedures, falsely represents that it complies with a buying broker's notification to cure a selling broker's failure to deliver shares by purchasing them in the open market.[41] That representation is false, appellants contend, because the NSCC actually executes those buying broker requests through the Stock Borrow Program, not the open market.

Assuming the truth of that allegation – that the NSCC's rules and procedures represent that the NSCC executes buy-in requests by directly going to the open market, but in truth, the Commission-approved Stock Borrow Program is utilized so that the NSCC never goes to the open market – it appears inextricably entwined with an assertion that respondents have violated their own Commission-approved rules governing the Stock Borrow Program.[42] That is, appellants appear to assert that, by

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[39] *See* cases cited *supra* note 38.

[40] *See Breliant v. Preferred Equities Corp.*, 109 Nev. 842, 845, 858 P.2d 1258, 1260 (1993).

[41] *See* National Securities Clearing Corp., 46 Fed.Reg. 41,892 (Aug. 18, 1981).

[42] *Cf. United States Department of Agriculture v. Hunter*, 171 F.2d 793, 795 (5th Cir.1949) (noting that, for sovereign immunity reasons, a governmental agency cannot be sued for carrying out its duties); *DL Capital Group v. Nasdaq Stock*

using the Stock Borrow Program, respondents do not act in accordance with their rules stating that they will fulfill the buying brokers' needs by going to the open market when so requested, even though the Stock Borrow Program is itself approved by the Commission.[43]

Appellants are, in essence, challenging the Commission-approved NSCC's rules' language, and thus, this claim is preempted for that reason.[44]

Appellants claim that respondents falsely represented, in the NSCC's rules and procedures manual, that the Stock Borrow Program satisfies delivery obligations by *borrowing* shares, since in reality those transactions constitute *sales*. Those transactions are sales, according to appellants, because when the

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Market, 409 F.3d 93, 97-98 (2d Cir.2005) (recognizing that as the Commission would be absolutely immune from suit for carrying out its functions, self-regulatory organizations have similar immunity when acting under authority that the Commission delegated to them); *id.* at 98 (providing that "allegations of bad faith, malice, and even fraud . . . cannot, except in the most unusual of circumstances, overcome *absolute* immunity").

Indeed, appellants conceded at oral argument that, to the extent their claims implicate rule violations, they may be preempted.

[43] This is so even though, in appellants' opening brief, they state that "[t]he district court correctly observed that [appellants] 'have not alleged that the NSCC violated any rules governing [the Stock Borrow Program].'"

[44] *Cf. Barnett Bank of Marion Cty., N.A.*, 517 U.S. at 31-32 (recognizing that when state law prohibits what a federal enactment permits, the federal enactment overrides the state law). *See generally Bantum v. American Stock Exchange, LLC*, 777 N.Y.S.2d 137, 140 (App.Div.2004) (noting that "the [Securities] Exchange Act [of 1934] establishes a scheme of regulation of the securities marketplace that combines self-regulation . . . with oversight and direct regulation by the [Commission]").

NSCC delivers the borrowed shares to the buyer, the buyer acquires "all right, title[,] and interest in the shares." That allegation appears premised on NRS 104.8501(2)(a), which provides that when an entry crediting a broker's account is made, that broker acquires a securities entitlement. "Securities entitlement" is defined in NRS 104.8102(l)(p) as rights and property interest in a security.

Those provisions notwithstanding, the Commission, in registering the NSCC, expressly approved the NSCC's rules and procedures, including the NSCC's description of the Stock Borrow Program as a procedure involving borrowing shares. Thus, to the extent that NRS 104.8501(2)(a) would require respondents to represent that the Stock Borrow Program satisfies stock delivery obligations through sales of shares, enforcement of this statutory provision would make it impossible for the NSCC to comply with the Commission-approved rules and procedures, describing the program as using borrowed shares. The NSCC could comply with both provisions only by amending its Commission-approved rules. Thus, the district court did not err when it determined that appellants' claims based on this purported misrepresentation were preempted.

Appellants further assert a claim concerning respondents' representation with regard to the efficiency of the clearing and settling process. Appellants allege that respondents falsely represent that they efficiently clear and settle securities transactions, when, according to appellants, respondents allow a selling broker's commitment to deliver the total number of shares sold to remain unfulfilled for prolonged periods. According to appellants, allowing delivery commitments to remain unfulfilled

for extended periods has negative market effects on those shares and artificially inflates the number of shares issued and outstanding. This claim also is preempted.

First, while respondents represent that they efficiently clear and settle securities transactions – indeed, Congress directed the Commission to regulate clearing agencies for that purpose[45] – the degree of efficiency necessary to satisfy that directive is not federally defined. Imposing any state law requirement for efficiency, which, in the absence of any federal standard, would be necessary before appellants could show that respondents have failed to efficiently clear and settle securities transactions here, would compel respondents to alter their federally approved manner of operating the Stock Borrow Program. Therefore, this claim is preempted.[46]

Second, any negative market effects, artificial inflation of shares, or so-called phantom shares that result from respondents not clearing and settling securities transactions as expediently as appellants would prefer, would, it appears, constitute an exploitable flaw inherent in the federally authorized system, preempting state law challenges to that flaw.[47]

Finally, with respect to appellants' misrepresentation claims, appellants challenge respondents'

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[45] *See* 15 U.S.C. § 78q-1(a).

[46] *Crosby*, 530 U.S. at 373 (noting that federal law preempts state law when the state law poses an obstacle to the accomplishment of Congress's objectives and purposes).

[47] *Id.* (recognizing that a federal law overrides any state law that frustrates the federal law's operation within its intended field).

representation regarding the number of shares that a lending broker actually retains in its DTC account after it has loaned shares of a given security. In essence, appellants contend that respondents' method of balancing the DTC and NSCC accounts and subaccounts created when a broker participates in the Stock Borrow Program overlooks the shares actually loaned and thus misrepresents the shares actually held by a lending broker in its DTC account. But like the previous allegation, respondents' method of balancing any accounts created while operating the Stock Borrow Program is a function of operating the Stock Borrow Program, a federally mandated and regulated system. Thus, this claim likewise is preempted.[48]

Appellants' non-misrepresentation claims

Appellants' remaining, non-misrepresentation claims include unfair trade practices in violation of NRS 598A.060, market manipulation in violation of NRS 90.580, conversion, intentional interference with contractual relations, breach of the implied covenant of good faith and fair dealing, and conspiracy. Those claims are preempted, as their mere descriptions, set forth below, demonstrate that they manifestly attack either the federally regulated operation or existence of the Stock Borrow Program.

Specifically, appellants' contention that respondents engaged in unfair trade practices in violation of NRS 598A.060 challenges respondents' representation that the Stock Borrow Program efficiently clears and settles trades and asserts that respondents "have illegally tied the Stock Borrow Program to the

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[48] *Id.*

separate and distinct functions of clearing and settling stock trades."

As regards appellants' NRS 90.580 market manipulation cause of action, appellants assert that, because respondents use the Stock Borrow Program as their predominate means of satisfying their share delivery obligations, instead of purchasing shares in the open market on a buying broker's notification, respondents conceal the demand for the stock of the company at issue. By concealing the demand for a company's stock, appellants assert, the market is misled concerning the demand for and value of that company's stock.

Appellants' conversion claim, as with one of the misrepresentation allegations above, alleges that the Stock Borrow Program does not involve borrowing, but rather creates a security entitlement. Because the Stock Borrow Program creates securities entitlements when Nanopierce shares are loaned, appellants contend, an actual sale is taking place and unauthorized, wrongful dominion is exercised over those shares.

Appellants' intentional interference with contractual relations claim asserts that operating the Stock Borrow Program interferes with Nanopierce's contractual relationships, based on its articles of incorporation, with its shareholders.

Appellants' claim for breach of the implied covenant of good faith and fair dealing alleges that, to the extent Nanopierce shares constitute a contract, the DTC, which holds those shares in its vaults in the name of its nominee, does not act in good faith with respect to those shares when placing them in the Stock Borrow Program.

Concerning appellants' conspiracy claim, they contend that respondents have conspired to use the Stock Borrow Program to manipulate and dilute Nanopierce's stock value.[49]

As set forth above, these non-misrepresentation claims overtly challenge the Stock Borrow Program and respondents' federally regulated operation of it. Therefore, those claims, like the misrepresentation-based claims, are preempted.[50]

Given the Securities Exchange Act's framework and provisions, in particular section 17A, any intent of Congress to occupy the legislative field of clearing and settling securities transactions is not "clear and manifest." Room exists for state laws to supplement that federal regulatory scheme, so long as any such state laws do not actually conflict with the federal law with respect to clearing and settling securities transactions. The question whether section 17A of the Securities Exchange Act and any regulations promulgated thereto – to the extent they concern clearing and settling securities transactions – pre-empt state law claims therefore turns on whether a

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[49] Notably, because respondents are a parent company and its subsidiaries, they have no separate legal existence; thus it appears "impossible for a civil conspiracy to have occurred." *Laxalt v. McClatchy*, 622 F.Supp. 737, 745-46 (D.Nev.1985) (citing *Corbit v. J.I. Case Company*, 424 P.2d 290, 295 n. 3 (Wash.1967)); *see also Collins v. Union Fed. Savings & Loan*, 99 Nev. 284, 662 P.2d 610 (1983) (recognizing that a corporation's agents or employees acting in their official capacities generally cannot conspire with the corporation).

[50] *See generally Dahl v. Charles Schwab & Co., Inc.*, 545 N.W.2d 918, 926 (Minn.1996) (recognizing that, given "the national import and possible effect" of any state law-based decision on a particular securities procedure, such decisions "are for the SEC and Congress").

party's compliance with both state and federal law requirements is impossible, or whether the Securities Exchange Act's purpose would be frustrated if state law applied.

Here, measuring appellants' state law claims against the Securities Exchange Act's framework with respect to clearing and settling securities transactions, and the federal statute's effects and purpose to allow the Commission to regulate and control a national system for clearing and settling securities transactions, reveals that appellants' claims conflict with Congress's regulatory scheme. That is, imposing the requirements implicated by appellants' state law claims, which they primarily base on allegations that respondents conceal flaws in a Commission-approved national system for clearing and settling securities transactions, frustrates Congress's objectives with respect to the clearing and settling regulatory scheme and renders adherence to both that regulatory scheme and state law impossible. Federal law thus preempts appellants' claims. Accordingly, as all of appellants' causes of action are preempted by federal enactments in the area of clearing and settling securities transaction, we conclude that the district court did not err in dismissing appellants' amended complaint, and we thus affirm the district court's order.

We concur: MAUPIN, C.J., GIBBONS, J., PARRAGUIRRE, J., and CHERRY, J.

HARDESTY, J., with whom DOUGLAS, J., agrees, concurring in part and dissenting in part:

The majority correctly determines that no field preemption exists in the general area of securities regulation and the specific area of clearing and settling securities transactions. I agree, moreover, with much of the majority's analysis regarding conflict preemption, which, as the majority notes, generally examines whether a party's compliance with both state and federal requirements is impossible or whether, in light of the federal law's purpose and intended effects, state law poses an obstacle to congressional objectives.[1] But in concluding, in light of such an examination, that all of appellants' state law causes of action conflict with federal law for a national system of clearing and settling securities transactions, the majority mischaracterizes appellants' allegation that the NSCC, in its rules and procedures, misrepresents that it complies with a buying broker's notification – *i.e.*, buy-in request – to cure a selling broker's failure to deliver shares by purchasing them in the open market, when instead, the NSCC utilizes the Stock Borrow Program. Thus, although I agree with the majority that federal law preempts most of appellants' claims, I would reverse the district court's order with respect to appellants' four causes of action based on that alleged misrepresentation and remand this matter for further proceedings.

The majority characterizes appellants' buy-in-request-based allegation as attacking the language of an NSCC, Commission-approved rule, which, if

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[1] *Crosby v. National Foreign Trade Council*, 530 U.S. 363, 372-73 (2000).

that characterization were accurate, unquestionably would be preempted. But that characterization is not accurate. Appellants specifically allege that respondents "misrepresented" to them that unsatisfied share delivery commitments would, on a broker's buy-in request, be cured by purchasing the necessary shares on the open market, when in fact, those unfulfilled obligations are "actually cured by borrowing shares from lending [brokers] through the Stock Borrow Program." In that allegation, appellants are not directly challenging any NSCC rule's language, but rather that respondents represent that they satisfy buy-in requests by purchasing shares in the open market, while instead using the Stock Borrow Program to satisfy buy-in requests. Determining whether respondents are liable on state law grounds for inaccurately representing how they executed buying brokers' notifications to purchase shares on the open market is not inconsistent with the Commission's approval of the Stock Borrow Program or the NSCC's rules, even if it indirectly causes respondents to choose whether to change those rules or face potential additional lawsuits.[2]

Indeed, it does not appear impossible for respondents to comply with Nevada's misrepresentation jurisprudence by accurately stating how notifications to purchase shares on the open market are executed while simultaneously complying with federal law controlling a national system for clearing and settling securities transactions. Nor does any such compliance appear to frustrate the accomplishment

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[2] *See Bates v. Dow Agrosciences LLC*, 544 U.S. 431, 445 (2005) (providing that "[a] requirement is a rule of law that must be obeyed; an event . . . that merely motivates an optional decision is not a requirement").

of Congress's objectives with respect to that regulatory scheme.

Therefore, as appellants' buy-in-request-based allegation does not conflict with federal law controlling a national system for clearing and settling securities transactions, I would reverse the district court's order with respect to appellants' causes of action based on that allegation and remand this matter for further proceedings.

I concur: DOUGLAS, J.

IN THE SECOND JUDICIAL DISTRICT COURT
OF THE STATE OF NEVADA
IN AND FOR THE COUNTY OF WASHOE

Case No. CV04-01079

NANOPIERCE TECHNOLOGIES, INC., ET AL.,
Plaintiff,

v.

THE DEPOSITORY TRUST AND CLEARING CORPORATION, ET AL.,
Defendants.

[Filed April 28, 2005]

ORDER

The court has read and considered the legal memorandum submitted in support of and opposition to Defendant's *Motion to Dismiss the Complaint* filed on July 30, 2004 and re-submitted March 4, 2005 as well as the oral arguments presented on February 16, 2005.

The dispute arises over the practice of clearing and settling securities through the Defendant institutions. Defendants are New York-based clearing and depository institutions explicitly authorized by the Securities and Exchange Commission (herein "SEC").[1] Plaintiffs claim that Defendants' federally

[1] The Depository Trust and Clearing Corporation (herein "DTCC") operates as a holding company, which consists of four subsidiaries: the Depository Trust Corporation (herein "DTC"), the National Securities Clearing Corporation (herein "NSCC"),

authorized clearing and settlement services, specifically the Stock Borrow Program (herein "SBP"), devalued Plaintiff Nanopierce's stock. Plaintiffs contend that SBP authorizes and facilitates naked short selling by market participants.[2] Defendants bring this motion to dismiss pursuant to NRCP 12(b)(5) arguing that Plaintiffs' claims fail because they are barred under the preemption doctrine.[3]

Motion to Dismiss

In considering a dismissal under NRCP 12(b)(5), the Court must construe the pleadings liberally and draw every fair inference in favor of the non-moving party. *Simpson v. Mars Inc.*, 113 Nev. 188, 929 P.2d 966 (1997). A complaint should not be dismissed for failure to state a claim unless it appears beyond a doubt that the plaintiff cannot prove any set of facts, which, if accepted by the jury, would entitle it to relief. *Id.* at 191. Nevada has a strong policy favoring

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the Fixed Income Clearing Corporation, and the Emerging Markets Clearing Corporation. The DTC is the nation's largest securities depository and clearinghouse for settlement of securities trading activity. The NSCC is a New York corporation that provides centralized clearance, settlement, and information services for virtually all broker-to-broker equity, corporate bond, municipal bond, exchange-traded funds and unit investment trades.

[2] The SBP, operated by NSCC, assists in settling transactions from which a delivery obligation remains open. Under the SBP, NSCC borrows members' shares of stock which are voluntarily loaned for the purpose of settling transactions where participants have not made sufficient shares available to satisfy delivery obligations. The SEC has explicitly approved the program.

[3] Although Defendants also assert that Plaintiffs' claims should fail on other grounds, the Court only addresses the preemption argument.

the resolution of disputes on the merits. *Yochum v. Davis*, 98 Nev. 484, 487, 653 P.2d 1215 (1982).

Defendants assert that Plaintiffs' causes of action should fail because the field has been so thoroughly occupied by federal law as to preempt state regulation of the federally authorized practices which are the subject of the complaint in this action. Whether a state law is preempted is a matter of congressional intent. If Congress intended to exercise its constitutional authority to supersede the laws of a state, the Supremacy Clause of the Constitution of the United States requires courts to follow federal law. *Levintin v. PaineWebber, Inc.*, 159 F.3d 698, 705 (1998). If the federal law does not contain explicit language regarding preemption, courts must consider whether the federal statute's structure and purpose, or non-specific statutory language, reveal a clear, implicit preemptive intent. *Barnett Bank of Marion County v. Nelson*, 517 U.S. 25, 116 S.Ct. 1103 (1996). Preemptive intent may be inferred when "the federal statute created a scheme of federal regulation 'so pervasive as to make reasonable the inference that Congress left no room for the states to supplement it.'" *Levintin*, 159 F.3d at 705 (quoting *Barnett Bank*, 517 U.S. at 31, 116 S.Ct. 1103).

Federal regulation of the securities industry, especially the clearing and depository institutions, is extensive. In 1975, Congress amended the Securities Exchange Act of 1934 by adding Section 17A. This amendment vested the United States Securities and Exchange Commission (herein "SEC") with the centralized decision-making authority and responsibility to oversee and regulate a uniform national market system for securities transactions. 15 U.S.C. 78q-1(a)(2)(A)(i). Accordingly, Congress granted the SEC

explicit authority to regulate clearing agencies like DTC and NSCC and to approve the regulations governing these agencies. 15 U.S.C. § 78q-1. The SBP is a component of NSCC's rules and was expressly approved by the SEC. SEC Release No. 34-17422, 46 Fed. Reg. 3104 (January 7, 1981).

As stated above, the SBP, which forms the basis of Plaintiffs' complaint, operates to assist NSCC in settling transactions for which a delivery obligation from the seller of securities of remains open. SEC Release No. 34-18027; 46 Fed. Reg. 41892 (August 18, 1981). The SBP operates in an automated fashion without the exercise of discretion by NSCC as to whether any particular open transaction should be covered by SBP. *National Securities Clearing Corp. Rules, Addendum C.* Each member of NSCC elects to participate in the SBP and permits its eligible stock to be made available for borrowing through the SBP program. *Id.* Therefore, if positions remain open and shares are voluntarily made available by members to fill such positions, the system will automatically fill the positions. SEC Release No 37-18027; 46 Fed. Reg. 41892 (August 18, 1981). If a member does not wish to make shares available, NSCC has no power to compel them to do so. *Id.*

As illustrated above, the federal government extensively regulates the securities industry. The SBP is an automated, non-discretionary process specifically approved by the SEC as a component of the nationwide stock transactions' clearing system. Therefore, the Court finds that federal law preempts Plaintiffs' claims for relief. Federal law explicitly permits the SBP to operate. Plaintiffs have not alleged that the NSCC violated any rules governing SBP. Therefore, state law may not be applied as to

impose damages on Defendants. To do this would be to forbid the Defendants from doing what the SEC authorized them to do.

Accordingly, and with good cause appearing, Defendants' *Motion to Dismiss the Complaint* is GRANTED.

DATED: This 27th day of April, 2005.

/s/ BRENT T. ADAMS
DISTRICT JUDGE

IN THE SUPREME COURT
OF THE STATE OF NEVADA

No. 45364

NANOPIERCE TECHNOLOGIES, INC., ET AL.,
Appellants,

v.

THE DEPOSITORY TRUST AND CLEARING CORPORATION, ET AL.,
Respondents.

[Filed November 5, 2007]

ORDER DENYING REHEARING

This is a petition for rehearing, styled "Petition for Rehearing and/or Clarification," of our September 20, 2007 opinion affirming a district court order that dismissed appellants' securities fraud action.

Contrary to the title of appellant's rehearing petition, appellants state that they are "not seek[ing] rehearing" of our September 20 opinion. Instead, appellants request that this court "remand this case to the district court with directions to permit [them] to seek leave to file a second amended complaint, thereby giving [them] the opportunity to allege state-law challenges" that do not conflict with the Securities Exchange Act of 1934 or any regulations promulgated thereto. But because we affirmed the district court's order dismissing appellants' complaint, effectively terminating this case, no portion of the case

remains to be litigated.[1] Second, leave to amend a complaint generally is within the district court's sound discretion,[2] and thus should have been sought in the district court in the first instance.[3]

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[1] See U.S. Ex Rel. Karvelas v. Melrose-Wakefield Hosp., 360 F.3d 220, 241 (1st Cir. 2004) (recognizing that the complaint's dismissal constitutes a final decision that "'ends the litigation on the merits and leaves nothing for the court to do but execute the judgment'" (quoting Acevedo-Villalobos v. Hernandez, 22 F.3d 384, 388 (1st Cir. 1994)); cf. Greene v. Dist. Ct., 115 Nev. 391, 393-94, 990 P.2d 184, 185 (1999) (recognizing with approval the policy favoring the finality of judgments and terminating litigation expeditiously); Zalk-Josephs Co. v. Wells Cargo, Inc., 81 Nev. 163, 400 P.2d 621 (1965) (noting that when a district court dismisses a case for failure to state a claim on which relief can be granted, and the plaintiff fails to request leave to amend the complaint, the dismissal constitutes a decision on the merits for res judicata purposes).

As appellants point out in their petition, the district court's order does not indicate whether its dismissal was with prejudice. But "in the absence of a clear statement to the contrary," the dismissal of a complaint for failure to state a claim on which relief can be granted "is presumed to be with prejudice." See U.S. Ex Rel. Karvelas, 360 F.3d at 241; see also Greene, 115 Nev. at 393, 990 P.2d at 185 (noting that "[f]ederal court interpretations of Federal Rules of Civil Procedure, as counterparts to the Nevada Rules of Civil Procedure, are persuasive but not controlling authority").

[2] See NRCP 15(a) (providing that "[a] party may amend the party's pleading once as a matter of course at any time before a responsive pleading is served . . . [o]therwise a party may amend the party's pleading only by leave of court"); Kantor v. Kantor, 116 Nev. 886, 891, 8 P.3d 825, 828 (2000) (noting that a motion for leave to amend under NRCP 15(a) is addressed to the district court's sound discretion).

[3] In opposing respondents' motion to dismiss the amended complaint based on NRCP 9(b), appellants asserted that any failure of their amended complaint to comply with that rule's pleading with particularity requirement "subjects the complaint to . . . dismissal with leave to amend." Appellants' request for

Additionally, even ignoring appellants' plain statement that they are "not seek[ing] rehearing" of our September 20 opinion, and instead construing appellants' petition as one to rehear the merits of our decision, rehearing is not warranted.[4]

It is so ORDERED.

/s/ MAUPIN, C.J.
Maupin

/s/ GIBBONS, J.
Gibbons

/s/ HARDESTY, J.
Hardesty

/s/ PARRAGUIRRE, J.
Parraguirre

/s/ DOUGLAS, J.
Douglas

/s/ CHERRY, J.
Cherry

/s/ SAITTA, J.
Saitta

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leave to amend unequivocally pertains only to the particularity of their fraud allegations, and thus is insufficient to constitute a request for leave to amend their complaint if the district court concluded, under NRCP 12(b)(5), that they failed to assert a claim on which relief could be granted. Indeed, appellants' rehearing petition fails to direct us to any request made in the district court that they be given leave to amend their complaint to assert viable state law claims.

[4] NRAP 40(c).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

Section 17A of the Securities Exchange Act of 1934, 15 U.S.C. § 78q-1, provides:

Sec. 78q-1. National system for clearance and settlement of securities transactions

(a) Congressional findings; facilitating establishment of system

(1) The Congress finds that –

(A) The prompt and accurate clearance and settlement of securities transactions, including the transfer of record ownership and the safeguarding of securities and funds related thereto, are necessary for the protection of investors and persons facilitating transactions by and acting on behalf of investors.

(B) Inefficient procedures for clearance and settlement impose unnecessary costs on investors and persons facilitating transactions by and acting on behalf of investors.

(C) New data processing and communications techniques create the opportunity for more efficient, effective, and safe procedures for clearance and settlement.

(D) The linking of all clearance and settlement facilities and the development of uniform standards and procedures for clearance and settlement will reduce unnecessary costs and increase the protection of investors and persons facilitating transactions by and acting on behalf of investors.

(2)(A) The Commission is directed, therefore, having due regard for the public interest, the protection of investors, the safeguarding of securities and funds, and maintenance of fair competition among brokers and dealers, clearing agencies, and transfer agents, to use its authority under this chapter –

(i) to facilitate the establishment of a national system for the prompt and accurate clearance and settlement of transactions in securities (other than exempt securities); and

(ii) to facilitate the establishment of linked or coordinated facilities for clearance and settlement of transactions in securities, securities options, contracts of sale for future delivery and options thereon, and commodity options;

in accordance with the findings and to carry out the objectives set forth in paragraph (1) of this subsection.

(B) The Commission shall use its authority under this chapter to assure equal regulation under this chapter of registered clearing agencies and registered transfer agents. In carrying out its responsibilities set forth in subparagraph (A)(ii) of this paragraph, the Commission shall coordinate with the Commodity Futures Trading Commission and consult with the Board of Governors of the Federal Reserve System.

(b) Registration of clearing agencies; application; determinations by Commission requisite to registration of applicant as clearing agency; denial of participation; discipline; summary proceedings

(1) Except as otherwise provided in this section, it shall be unlawful for any clearing agency, unless reg-

istered in accordance with this subsection, directly or indirectly, to make use of the mails or any means or instrumentality of interstate commerce to perform the functions of a clearing agency with respect to any security (other than an exempted security). The Commission, by rule or order, upon its own motion or upon application, may conditionally or unconditionally exempt any clearing agency or security or any class of clearing agencies or securities from any provisions of this section or the rules or regulations thereunder, if the Commission finds that such exemption is consistent with the public interest, the protection of investors, and the purposes of this section, including the prompt and accurate clearance and settlement of securities transactions and the safeguarding of securities and funds. A clearing agency or transfer agent shall not perform the functions of both a clearing agency and a transfer agent unless such clearing agency or transfer agent is registered in accordance with this subsection and subsection (c) of this section.

(2) A clearing agency may be registered under the terms and conditions hereinafter provided in this subsection and in accordance with the provisions of section 78s(a) of this title, by filing with the Commission an application for registration in such form as the Commission, by rule, may prescribe containing the rules of the clearing agency and such other information and documents as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the prompt and accurate clearance and settlement of securities transactions.

(3) A clearing agency shall not be registered unless the Commission determines that –

(A) Such clearing agency is so organized and has the capacity to be able to facilitate the prompt and accurate clearance and settlement of securities transactions and derivative agreements, contracts, and transactions for which it is responsible, to safeguard securities and funds in its custody or control or for which it is responsible, to comply with the provisions of this chapter and the rules and regulations thereunder, to enforce (subject to any rule or order of the Commission pursuant to section 78q(d) or 78s(g)(2) of this title) compliance by its participants with the rules of the clearing agency, and to carry out the purposes of this section.

(B) Subject to the provisions of paragraph (4) of this subsection, the rules of the clearing agency provide that any (i) registered broker or dealer, (ii) other registered clearing agency, (iii) registered investment company, (iv) bank, (v) insurance company, or (vi) other person or class of persons as the Commission, by rule, may from time to time designate as appropriate to the development of a national system for the prompt and accurate clearance and settlement of securities transactions may become a participant in such clearing agency.

(C) The rules of the clearing agency assure a fair representation of its shareholders (or members) and participants in the selection of its directors and administration of its affairs. (The Commission may determine that the representation of participants is fair if they are afforded a reasonable opportunity to acquire voting stock of the clearing agency, directly or indirectly, in reasonable proportion to their use of such clearing agency.)

(D) The rules of the clearing agency provide for the equitable allocation of reasonable dues, fees, and other charges among its participants.

(E) The rules of the clearing agency do not impose any schedule of prices, or fix rates or other fees, for services rendered by its participants.

(F) The rules of the clearing agency are designed to promote the prompt and accurate clearance and settlement of securities transactions and, to the extent applicable, derivative agreements, contracts, and transactions, to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible, to foster cooperation and coordination with persons engaged in the clearance and settlement of securities transactions, to remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and, in general, to protect investors and the public interest; and are not designed to permit unfair discrimination in the admission of participants or among participants in the use of the clearing agency, or to regulate by virtue of any authority conferred by this chapter matters not related to the purposes of this section or the administration of the clearing agency.

(G) The rules of the clearing agency provide that (subject to any rule or order of the Commission pursuant to section 78q(d) or 78s(g)(2) of this title) its participants shall be appropriately disciplined for violation of any provision of the rules of the clearing agency by expulsion, suspension, limitation of activities, functions, and operations, fine, censure, or any other fitting sanction.

(H) The rules of the clearing agency are in accordance with the provisions of paragraph (5) of this subsection, and, in general, provide a fair procedure with respect to the disciplining of participants, the denial of participation to any person seeking participation therein, and the prohibition or limitation by the clearing agency of any person with respect to access to services offered by the clearing agency.

(I) The rules of the clearing agency do not impose any burden on competition not necessary or appropriate in furtherance of the purposes of this chapter.

(4)(A) A registered clearing agency may, and in cases in which the Commission, by order, directs as appropriate in the public interest shall, deny participation to any person subject to a statutory disqualification. A registered clearing agency shall file notice with the Commission not less than thirty days prior to admitting any person to participation, if the clearing agency knew, or in the exercise of reasonable care should have known, that such person was subject to a statutory disqualification. The notice shall be in such form and contain such information as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(B) A registered clearing agency may deny participation to, or condition the participation of, any person if such person does not meet such standards of financial responsibility, operational capability, experience, and competence as are prescribed by the rules of the clearing agency. A registered clearing agency may examine and verify the qualifications of an applicant to be a participant in accordance with

procedures established by the rules of the clearing agency.

(5)(A) In any proceeding by a registered clearing agency to determine whether a participant should be disciplined (other than a summary proceeding pursuant to subparagraph (C) of this paragraph), the clearing agency shall bring specific charges, notify such participant of, and give him an opportunity to defend against such charges, and keep a record. A determination by the clearing agency to impose a disciplinary sanction shall be supported by a statement setting forth –

(i) any act or practice in which such participant has been found to have engaged, or which such participant has been found to have omitted;

(ii) the specific provisions of the rules of the clearing agency which any such act or practice, or omission to act, is deemed to violate; and

(iii) the sanction imposed and the reasons therefor.

(B) In any proceeding by a registered clearing agency to determine whether a person shall be denied participation or prohibited or limited with respect to access to services offered by the clearing agency, the clearing agency shall notify such person of, and give him an opportunity to be heard upon, the specific grounds for denial or prohibition or limitation under consideration and keep a record. A determination by the clearing agency to deny participation or prohibit or limit a person with respect to access to services offered by the clearing agency shall be supported by a statement setting forth the specific grounds on which the denial or prohibition or limitation is based.

(C) A registered clearing agency may summarily suspend and close the accounts of a participant who (i) has been and is expelled or suspended from any self-regulatory organization, (ii) is in default of any delivery of funds or securities to the clearing agency, or (iii) is in such financial or operating difficulty that the clearing agency determines and so notifies the appropriate regulatory agency for such participant that such suspension and closing of accounts are necessary for the protection of the clearing agency, its participants, creditors, or investors. A participant so summarily suspended shall be promptly afforded an opportunity for a hearing by the clearing agency in accordance with the provisions of subparagraph (A) of this paragraph. The appropriate regulatory agency for such participant, by order, may stay any such summary suspension on its own motion or upon application by any person aggrieved thereby, if such appropriate regulatory agency determines summarily or after notice and opportunity for hearing (which hearing may consist solely of the submission of affidavits or presentation of oral arguments) that such stay is consistent with the public interest and protection of investors.

(6) No registered clearing agency shall prohibit or limit access by any person to services offered by any participant therein.

(7)(A) A clearing agency that is regulated directly or indirectly by the Commodity Futures Trading Commission through its association with a designated contract market for security futures products that is a national securities exchange registered pursuant to section 78f(g) of this title, and that would be required to register pursuant to paragraph (1) of this subsection only because it performs the functions of a

clearing agency with respect to security futures products effected pursuant to the rules of the designated contract market with which such agency is associated, is exempted from the provisions of this section and the rules and regulations thereunder, except that if such a clearing agency performs the functions of a clearing agency with respect to a security futures product that is not cash settled, it must have arrangements in place with a registered clearing agency to effect the payment and delivery of the securities underlying the security futures product.

(B) Any clearing agency that performs the functions of a clearing agency with respect to security futures products must coordinate with and develop fair and reasonable links with any and all other clearing agencies that perform the functions of a clearing agency with respect to security futures products, in order to permit, as of the compliance date (as defined in section 78f(h)(6)(C)[1] of this title), security futures products to be purchased on one market and offset on another market that trades such products.

(8) A registered clearing agency shall be permitted to provide facilities for the clearance and settlement of any derivative agreements, contracts, or transactions that are excluded from the Commodity Exchange Act [7 U.S.C. 1 et seq.], subject to the requirements of this section and to such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this chapter.

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[1] So in original. Probably should be "section 78f(h)(7)(C)".

(c) Registration of transfer agents

(1) Except as otherwise provided in this section, it shall be unlawful for any transfer agent, unless registered in accordance with this section, directly or indirectly, to make use of the mails or any means or instrumentality of interstate commerce to perform the function of a transfer agent with respect to any security registered under section 78*l* of this title or which would be required to be registered except for the exemption from registration provided by subsection (g)(2)(B) or (g)(2)(G) of that section. The appropriate regulatory agency, by rule or order, upon its own motion or upon application, may conditionally or unconditionally exempt any person or security or class of persons or securities from any provision of this section or any rule or regulation prescribed under this section, if the appropriate regulatory agency finds (A) that such exemption is in the public interest and consistent with the protection of investors and the purposes of this section, including the prompt and accurate clearance and settlement of securities transactions and the safeguarding of securities and funds, and (B) the Commission does not object to such exemption.

(2) A transfer agent may be registered by filing with the appropriate regulatory agency for such transfer agent an application for registration in such form and containing such information and documents concerning such transfer agent and any persons associated with the transfer agent as such appropriate regulatory agency may prescribe as necessary or appropriate in furtherance of the purposes of this section. Except as hereinafter provided, such registration shall become effective 45 days after receipt of such application by such appropriate regulatory

agency or within such shorter period of time as such appropriate regulatory agency may determine.

(3) The appropriate regulatory agency for a transfer agent, by order, shall deny registration to, censure, place limitations on the activities, functions, or operations of, suspend for a period not exceeding 12 months, or revoke the registration of such transfer agent, if such appropriate regulatory agency finds, on the record after notice and opportunity for hearing, that such denial, censure, placing of limitations, suspension, or revocation is in the public interest and that such transfer agent, whether prior or subsequent to becoming such, or any rson associated with such transfer agent, whether prior or subsequent to becoming so associated –

(A) has committed or omitted any act, or is subject to an order or finding, enumerated in subparagraph (A), (D), (E), (H), or (G) of paragraph (4) of section 78o(b) of this title, has been convicted of any offense specified in subparagraph (B) of such paragraph (4) within ten years of the commencement of the proceedings under this paragraph, or is enjoined from any action, conduct, or practice specified in subparagraph (C) of such paragraph (4); or

(B) is subject to an order entered pursuant to subparagraph (C) of paragraph (4) of this subsection barring or suspending the right of such person to be associated with a transfer agent.

(4)(A) Pending final determination whether any registration by a transfer agent under this subsection shall be denied, the appropriate regulatory agency for such transfer agent, by order, may postpone the effective date of such registration for a period not to exceed fifteen days, but if, after notice and oppor-

tunity for hearing (which may consist solely of affidavits and oral arguments), it shall appear to such appropriate regulatory agency to be necessary or appropriate in the public interest or for the protection of investors to postpone the effective date of such registration until final determination, such appropriate regulatory agency shall so order. Pending final determination whether any registration under this subsection shall be revoked, such appropriate regulatory agency, by order, may suspend such registration, if such suspension appears to such appropriate regulatory agency, after notice and opportunity for hearing, to be necessary or appropriate in the public interest or for the protection of investors.

(B) A registered transfer agent may, upon such terms and conditions as the appropriate regulatory agency for such transfer agent deems necessary or appropriate in the public interest, for the protection of investors, or in furtherance of the purposes of this section, withdraw from registration by filing a written notice of withdrawal with such appropriate regulatory agency. If such appropriate regulatory agency finds that any transfer agent for which it is the appropriate regulatory agency, is no longer in existence or has ceased to do business as a transfer agent, such appropriate regulatory agency, by order, shall cancel or deny the registration.

(C) The appropriate regulatory agency for a transfer agent, by order, shall censure or place limitations on the activities or functions of any person associated, seeking to become associated, or, at the time of the alleged misconduct, associated or seeking to become associated with the transfer agent, or suspend for a period not exceeding twelve months or bar any such person from being associated with the transfer

agent, if the appropriate regulatory agency finds, on the record after notice and opportunity for hearing, that such censure, placing of limitations, suspension, or bar is in the public interest and that such person has committed or omitted any act, or is subject to an order or finding, enumerated in subparagraph (A), (D), (E), (H), or (G) or[1] paragraph (4) of section 78o(b) of this title, has been convicted of any offense specified in subparagraph (B) of such paragraph (4) within ten years of the commencement of the proceedings under this paragraph, or is enjoined from any action, conduct, or practice specified in subparagraph (C) of such paragraph (4). It shall be unlawful for any person as to whom such an order suspending or barring him from being associated with a transfer agent is in effect willfully to become, or to be, associated with a transfer agent without the consent of the appropriate regulatory agency that entered the order and the appropriate regulatory agency for that transfer agent. It shall be unlawful for any transfer agent to permit such a person to become, or remain, a person associated with it without the consent of such appropriate regulatory agencies, if the transfer agent knew, or in the exercise of reasonable care should have known, of such order. The Commission may establish, by rule, procedures by which a transfer agent reasonably can determine whether a person associated or seeking to become associated with it is subject to any such order, and may require, by rule, that any transfer agent comply with such procedures.

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[1] So in original. Should probably be "of".

(d) Activities of clearing agencies and transfer agents; enforcement by appropriate regulatory agencies

(1) No registered clearing agency or registered transfer agent shall, directly or indirectly, engage in any activity as clearing agency or transfer agent in contravention of such rules and regulations (A) as the Commission may prescribe as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this chapter, or (B) as the appropriate regulatory agency for such clearing agency or transfer agent may prescribe as necessary or appropriate for the safeguarding of securities and funds.

(2) With respect to any clearing agency or transfer agent for which the Commission is not the appropriate regulatory agency, the appropriate regulatory agency for such clearing agency or transfer agent may, in accordance with section 1818 of title 12, enforce compliance by such clearing agency or transfer agent with the provisions of this section, sections 78q and 78s of this title, and the rules and regulations thereunder. For purposes of the preceding sentence, any violation of any such provision shall constitute adequate basis for the issuance of an order under section 1818(b) or 1818(c) of title 12, and the participants in any such clearing agency and the persons doing business with any such transfer agent shall be deemed to be "depositors" as that term is used in section 1818(c) of title 12.

(3)(A) With respect to any clearing agency or transfer agent for which the Commission is not the appropriate regulatory agency, the Commission and the appropriate regulatory agency for such clearing agency or transfer agent shall consult and cooperate

with each other, and, as may be appropriate, with State banking authorities having supervision over such clearing agency or transfer agent toward the end that, to the maximum extent practicable, their respective regulatory responsibilities may be fulfilled and the rules and regulations applicable to such clearing agency or transfer agent may be in accord with both sound banking practices and a national system for the prompt and accurate clearance and settlement of securities transactions. In accordance with this objective –

(i) the Commission and such appropriate regulatory agency shall, at least fifteen days prior to the issuance for public comment of any proposed rule or regulation or adoption of any rule or regulation concerning such clearing agency or transfer agent, consult and request the views of the other; and

(ii) such appropriate regulatory agency shall assume primary responsibility to examine and enforce compliance by such clearing agency or transfer agent with the provisions of this section and sections 78q and 78s of this title.

(B) Nothing in the preceding subparagraph or elsewhere in this chapter shall be construed to impair or limit (other than by the requirement of notification) the Commission's authority to make rules under any provision of this chapter or to enforce compliance pursuant to any provision of this chapter by any clearing agency, transfer agent, or person associated with a transfer agent with the provisions of this chapter and the rules and regulations thereunder.

(4) Nothing in this section shall be construed to impair the authority of any State banking authority or other State or Federal regulatory authority having

jurisdiction over a person registered as a clearing agency, transfer agent, or person associated with a transfer agent, to make and enforce rules governing such person which are not inconsistent with this chapter and the rules and regulations thereunder.

(5) A registered transfer agent may not, directly or indirectly, engage in any activity in connection with the guarantee of a signature of an endorser of a security, including the acceptance or rejection of such guarantee, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest, for the protection of investors, to facilitate the equitable treatment of financial institutions which issue such guarantees, or otherwise in furtherance of the purposes of this chapter.

(e) Physical movement of securities certificates

The Commission shall use its authority under this chapter to end the physical movement of securities certificates in connection with the settlement among brokers and dealers of transactions in securities consummated by means of the mails or any means or instrumentalities of interstate commerce.

(f) Rules concerning transfer of securities and rights and obligations of involved or affected parties

(1) Notwithstanding any provision of State law, except as provided in paragraph (3), if the Commission makes each of the findings described in paragraph (2)(A), the Commission may adopt rules concerning –

(A) the transfer of certificated or uncertificated securities (other than government securities issued pursuant to chapter 31 of title 31 or securities

otherwise processed within a book-entry system operated by the Federal Reserve banks pursuant to a Federal book-entry regulation) or limited interests (including security interests) therein; and

(B) rights and obligations of purchasers, sellers, owners, lenders, borrowers, and financial intermediaries (including brokers, dealers, banks, and clearing agencies) involved in or affected by such transfers, and the rights of third parties whose interests in such securities devolve from such transfers.

(2)(A) The findings described in this paragraph are findings by the Commission that –

(i) such rule is necessary or appropriate for the protection of investors or in the public interest and is reasonably designed to promote the prompt, accurate, and safe clearance and settlement of securities transactions;

(ii) in the absence of a uniform rule, the safe and efficient operation of the national system for clearance and settlement of securities transactions will be, or is, substantially impeded; and

(iii) to the extent such rule will impair or diminish, directly or indirectly, rights of persons specified in paragraph (1)(B) under State law concerning transfers of securities (or limited interests therein), the benefits of such rule outweigh such impairment or diminution of rights.

(B) In making the findings described in subparagraph (A), the Commission shall give consideration to the recommendations of the Advisory Committee established under paragraph (4), and it shall consult with and consider the views of the Secretary of the Treasury and the Board of Governors of the Federal

Reserve System. If the Secretary of the Treasury objects, in writing, to any proposed rule of the Commission on the basis of the Secretary's view on the issues described in clauses (i), (ii), and (iii) of subparagraph (A), the Commission shall consider all feasible alternatives to the proposed rule, and it shall not adopt any such rule unless the Commission makes an explicit finding that the rule is the most practicable method for achieving safe and efficient operation of the national clearance and settlement system.

(3) Any State may, prior to the expiration of 2 years after the Commission adopts a rule under this subsection, enact a statute that specifically refers to this subsection and the specific rule thereunder and establishes, prospectively from the date of enactment of the State statute, a provision that differs from that applicable under the Commission's rule.

(4)(A) Within 90 days after October 16, 1990, the Commission shall (and at such times thereafter as the Commission may determine, the Commission may), after consultation with the Secretary of the Treasury and the Board of Governors of the Federal Reserve System, establish an advisory committee under the Federal Advisory Committee Act (5 U.S.C. App.). The Advisory Committee shall be directed to consider and report to the Commission on such matters as the Commission, after consultation with the Secretary of the Treasury and the Board of Governors of the Federal Reserve System, determines, including the areas, if any, in which State commercial laws and related Federal laws concerning the transfer of certificated or uncertificated securities, limited interests (including security interests) in such securities, or the creation or perfection of

security interests in such securities do not provide the necessary certainty, uniformity, and clarity for purchasers, sellers, owners, lenders, borrowers, and financial intermediaries concerning their respective rights and obligations.

(B) The Advisory Committee shall consist of 15 members, of which –

(i) 11 shall be designated by the Commission in accordance with the Federal Advisory Committee Act; and

(ii) 2 each shall be designated by the Board of Governors of the Federal Reserve System and the Secretary of the Treasury.

(C) The Advisory Committee shall conduct its activities in accordance with the Federal Advisory Committee Act. Within 6 months of its designation, or such longer time as the Commission may designate, the Advisory Committee shall issue a report to the Commission, and shall cause copies of that report to be delivered to the Secretary of the Treasury and the Chairman of the Board of Governors of the Federal Reserve System.

Section 28(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78bb(a), provides:

Sec. 78bb. Effect on existing law

(a) Addition of rights and remedies; recovery of actual damages; State securities commissions

Except as provided in subsection (f) of this section, the rights and remedies provided by this chapter shall be in addition to any and all other rights and remedies that may exist at law or in equity; but no person permitted to maintain a suit for damages under the provisions of this chapter shall recover, through satisfaction of judgment in one or more actions, a total amount in excess of his actual damages on account of the act complained of. Except as otherwise specifically provided in this chapter, nothing in this chapter shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of this chapter or the rules and regulations thereunder. No State law which prohibits or regulates the making or promoting of wagering or gaming contracts, or the operation of "bucket shops" or other similar or related activities, shall invalidate any put, call, straddle, option, privilege, or other security subject to this chapter, or apply to any activity which is incidental or related to the offer, purchase, sale, exercise, settlement, or closeout of any such security. No provision of State law regarding the offer, sale, or distribution of securities shall apply to any transaction in a security futures product, except that this sentence shall not be construed as limiting any State antifraud law of general applicability.

Section 16(a) of the Securities Act of 1933, 15 U.S.C. § 77p(a), provides:

Sec. 77p. Additional remedies; limitation on remedies

(a) Remedies additional

Except as provided in subsection (b) of this section, the rights and remedies provided by this subchapter shall be in addition to any and all other rights and remedies that may exist at law or in equity.

Supreme Court of the United States
Office of the Clerk
Washington, DC 20543-0001

WILLIAM K. SUTER
Clerk of the Court
(202) 479-3011

December 14, 2007

Mr. David C. Frederick
Kellogg, Huber, Hansen, Todd, Evans & Figel, P.L.L.C.
1615 M Street, N.W.
Suite 400
Washington, DC 20036

Re: NanoPierce Technologies, Inc., et al.
v. Depository Trust and Clearing Corporation, et al.
Application No. 07A485

Dear Mr. Frederick:

The application for an extension of time within which to file a petition for a writ of certiorari in the above-entitled case has been presented to Justice Kennedy, who on December 14, 2007 extended the time to and including February 4, 2008.

This letter has been sent to those designated on the attached notification list.

Sincerely,

William K. Suter, Clerk
by /s/ GAIL JOHNSON

Gail Johnson
Case Analyst

[attached notification list omitted]

FILED
APR 3 - 2008
OFFICE OF THE CLERK
SUPREME COURT, U.S.

No. 07-1006

IN THE

Supreme Court of the United States

NANOPIERCE TECHNOLOGIES, INC. (N/K/A VYTA CORP.), KATHY-KNIGHT MCCONNELL, HELEN KOLADA, MAUREEN O'SULLIVAN, JANE SEITZ, STEPHEN SEITZ, AND JAMES STOCK,

Petitioners,

v.

DEPOSITORY TRUST AND CLEARING CORPORATION, DEPOSITORY TRUST COMPANY, AND NATIONAL SECURITIES CLEARING CORPORATION,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF NEVADA

BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether the Nevada Supreme Court erred in holding that petitioners' challenge to respondents' Stock Borrow Program, a component of the uniform SEC-approved system for clearing and settling the nation's securities transactions – a challenge cast as state law misrepresentation claims but actually rooted in alleged inherent defects in the program itself – would stand as an obstacle to the SEC-approved program and is therefore subject to conflicts preemption.

CORPORATE DISCLOSURE STATEMENT

Respondent, The Depository Trust & Clearing Corporation has no parent corporation and no publicly held company owns 10% or more of its stock. It is the sole owner of all other respondents.

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INTRODUCTION

The decision of the Supreme Court of Nevada, upholding the dismissal of the amended complaint on grounds of conflicts preemption, is one of several decisions (none of which are cited in the Petition) consistently applying the preemption doctrine to dismiss purported state law attacks on the Stock Borrow Program ("SBP"), which respondents operate under rules approved by the U.S. Securities and Exchange Commission ("SEC").[1]

---

[1] Respondents are The Depository Trust & Clearing Corporation and its subsidiaries (collectively, "DTCC"). Co-counsel for petitioners have unsuccessfully brought several actions asserting state law claims against respondents substantively identical to those presented here. Each has been dismissed on grounds of federal preemption. *See Pet Quarters, Inc. v. DTCC*, 4:04-cv-1528, 2008 U.S. Dist. LEXIS 15316 (E.D.Ark. Feb. 25, 2008) (dismissing challenge to SBP on grounds of federal preemption); *Capece v. DTCC*, Case No. 05-80498, 2005 U.S. Dist. LEXIS 42039 (S.D. Fla. Oct. 11, 2005) (same); *Whistler Investments, Inc. v. DTCC*, Case No. CV-S-05-0634-RJC (PAL) (D. Nev. May 24, 2006) (same), appeal in Docket No. 06-16088 argued March 10, 2008 (9th Cir.).

The SBP was also challenged in *Sporn v. Elgindy*, 2:04-cv-06417-R-PJW (C.D. Cal. July 26, 2005). Respondents moved to dismiss, *inter alia*, on grounds of federal preemption. By order filed July 25, 2005, the third amended complaint was summarily dismissed. *See also X-Clearing Corporation v. Depository Trust Corp.*, 03 CV 1169 (Dist. Ct., Denver, Col. Oct. 3, 2003) (dismissing as preempted claims by a company alleged to be the victim of naked short selling that it should be permitted to "exit" its publicly issued shares from DTCC's depository facility).

(Cont'd)

The SBP is a component of the uniform system for clearing and settling the nation's securities transactions, established pursuant to Section 17A of the 1975 Amendments to the Securities Exchange Act of 1934 ("Section 17A"), 15 U.S.C. § 78q-1. As explained by the SEC to the court below in its *amicus curiae* submission, the premise of petitioners' claims is wholly inconsistent with the SEC's approval of the SBP pursuant to Section 17A, and allowance of petitioners' claims would frustrate Congress's express goals in establishing the uniform "National Clearance and Settlement System" under SEC supervision. 15 U.S.C. § 78q-1(a)(2)(A)(i).[2]

The holding that petitioners' claims are preempted poses no conflict with any of the court decisions identified by petitioners, including *Bates v. Dow Agrosciences LLC*, 544 U.S. 431 (2005).

(Cont'd)

Other cases including challenges to the SBP were withdrawn or abandoned. *See Capece, Jr. v. Depository Trust*, Case No. 04-8043 (S.D. Fla. April 28, 2004) (withdrawn); *Nutek Inc. v. Ameritrade, Inc., et al.*, 2:03-cv-00321-PMP-RJJ (D. Nev. Aug. 3, 2004) (withdrawn against DTCC defendants after filing of motion to dismiss); *Williamson v. Goldman, Sachs & Co. et al.*, 3:03-cv-00057-HDM-RAM (D. Nev.) (filed but never served upon named DTCC defendants); *Genemax Corporation v. Knight Securities, LP., et al.*, 3:02-cv-00509-ECR-RAM (D. Nev.) (same).

[2] The SEC's *amicus* brief, urging affirmance on grounds of conflicts preemption, was filed in the Nevada Supreme Court by Order dated March 30, 2006. That brief is available on the SEC's website at www.sec.gov/litigation/briefs/nanopiercesec brief.pdf. The SEC filed a similar brief with the Ninth Circuit in the pending appeal in *Whistler Investments*.

Although styled as a state law misrepresentation case to try to avoid the preemptive effect of the SEC's approval of the challenged program, any reading of the complaint makes plain that it is a facial attack on the uniform, national system for clearance and settlement of securities transactions, and as such preempted.[3] Petitioners (collectively, "Nanopierce"), claim that the SBP, approved by the SEC in 1981, has certain inherent defects – the creation of "phantom shares" that harm the marketplace – and that respondents failed to disclose the SBP's "real effect" to the investing public. (Pet. 15.) As the Nevada Supreme Court held (Pet. App. 17A-21A), the complained-of "misrepresentations" are simply Nanopierce's characterizations of the SBP, which are wholly contrary to the SEC's own characterizations and assessment in approving the program pursuant to its Congressional mandate.

Nanopierce did not allege that any misrepresentations were made regarding the company. Nor did Nanopierce allege that the SBP operates differently with respect to Nanopierce stock than it does with respect to the stock of any of the thousands of other companies for which transactions are cleared and settled by DTCC. The alleged "misrepresentations" at issue did not arise in connection with any Nanopierce-specific conduct. Rather, petitioners challenge the uniform and automated operations of the SBP under SEC-approved rules and oversight, and in particular the discrepancy

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[3] The complaint contained not only claims concerning alleged misrepresentations and omissions but also what the Supreme Court of Nevada termed "non-misrepresentation claims," all of which were found preempted. Petitioners have abandoned the latter. (*See* Pet. 19 n.17.)

between the descriptions of the program contained in those approved rules and the pejorative characterizations contradicting the rules that petitioners insist state law requires respondents to disseminate.

Underlying this case and the several others exactly like it is Nanopierce's challenge to a trading strategy known as "naked short selling." (Pet. 14.) Naked short selling is illegal and subject to regulation by the SEC. *See Amendments to Regulation SHO*, 72 Fed. Reg. 45544 (Aug. 14, 2007) (adopting final rule amending Regulation SHO, 17 C.F.R. Part 242.200, 203; *"Naked" Short Selling Anti-Fraud Rule*, SEC Rel. 34-57511 (March 17, 2008) (proposed new Rule 10b-21, addressing naked short-selling, published for notice and comment). Nonetheless, through a series of facial attacks on the SEC-approved SBP (presented as garden variety misrepresentation claims), Nanopierce and plaintiffs in the companion cases have sought to impose the financial responsibility for damages allegedly caused by such naked short selling in the marketplace on the post-trade national clearance and settlement system.[4]

None of the inapposite cases cited by petitioners in arguing that state-law claims have "regularly been adjudicated" against clearance and settlement activities (Pet. 6 and n.2) addressed a frontal challenge to

[4] The parties responsible for alleged fraudulent transactions in Nanopierce stock have not been sued in this action, but were sued in another action, *Nanopierce Technologies, Inc. v. Harvest Court LLC, et al.*, No. 02-CV-0767 (S.D.N.Y.). The district court in that case recently entered summary judgment dismissing each of Nanopierce's claims. 2008 U.S. Dist. LEXIS 6225 (S.D.N.Y. Jan. 28, 2008).

federally-approved activities, as is the case here, or indeed addressed any preemption defenses at all. Rather, the cases cited by petitioners all dealt with ordinary-course business disputes regarding specific transactions between DTCC and the respective plaintiffs – not claims (such as here) effectively attacking a component of the federally-approved clearance and settlement system.[5] *Compare* cases cited nn. 1 and 5 *supra; cf. American Agricultural Movement, Inc, v. Board of Trade of Chicago*, 977 F.2d 1147 (7th Cir. 1992); *Myers v. Merrill Lynch & Co.*, No. C-98-3532, 1999 WL 696082, at *8-9 (N.D. Cal. Aug. 23, 1999), *aff'd*, 249 F.3d 1087 (9th Cir. 2001).

Nanopierce has cited no case, and DTCC is aware of none, that has ever applied state law to impose damages or injunctive relief against an SEC-approved component of the National Clearance and Settlement System. To the contrary, there is an unbroken line of cases in which

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[5] The exception is *Goldstein v. Depository Trust Corporation*, January Term, 1989, No. 3300 (Phil. Ct. Common Pleas), in which petitioners cite a long-superseded interim ruling (717 A.2d 1063 (Pa. Super. Ct 1998)) said to reflect an adjudication of state law claims in connection with the clearance of securities. (Pet. 6 n.2.) In fact, apparently unknown to petitioners, *Goldstein* was subsequently dismissed on preemption grounds because, as here, the challenged activity was taken pursuant to The Depository Trust Company's SEC-approved rules. (Unreported decision, December 28, 2001, copy provided to petitioners herewith.) The remaining cases relied upon by petitioners in arguing that relevant "state law claims have regularly been adjudicated" (Pet. 6, n.2) were decided long before Congress enacted the National Clearance and Settlement System in 1975 and long before respondents had even come into existence, and are completely inapposite.

the courts have recognized the primacy of the SEC in regulating the uniform post-trade securities handling process and invoked the preemption doctrine to dismiss state law claims. *See* n.1 *supra*. Those cases make plain that Nanopierce's effort to create the spectre of a state judiciary in disarray and in need of this Court's intervention is baseless. Nothing about this case merits this Court's attention.

STATEMENT OF THE CASE

1. In the late 1960s, Wall Street experienced a "paperwork crisis," as the volume of securities transactions (a tiny percentage of today's volumes) overwhelmed the industry's ability to process transactions. *See* Sen. Rep. No. 94-75, 1975 U.S.C.C.A.N. 179 (Apr. 14, 1975) (hereafter "Sen. Rep.") at 183. Congress recognized that paper indicia of securities ownership was incompatible with the modern securities industry: "A second major purpose of the legislation [Section 17A] is to initiate concrete steps toward the elimination of the negotiable stock certificate as a means of transferring securities." *Id.* at 236-37; *see also* H.R. Conf. Rep. No. 94-229 (May 19, 1975) at 92-93.

Congress's solution to the paperwork crisis and the fractured nature of the post-trade securities handling system (*see* Sen. Rep. at 183-84) was embodied in Section 17A, whose principal goal was "the development of *uniform standards and procedures for clearance and settlement* [of securities transactions] . . . ." 15 U.S.C. § 78q-1(a)(1)(D) (emphasis added); *see also* 15 U.S.C. § 78q-1(a)(1)(A) (Section 17A designed to create a

uniform national system for the prompt and accurate clearance and settlement of securities transactions).[6]

Section 17A vested the SEC with the centralized authority to preside over the National Clearance and Settlement System in order to increase efficiency and reduce risk. 15 U.S.C. § 78q-1(a)(2)(A)(i); *see Self-Regulatory Organizations: The Depository Trust Company: Order Granting Approval of a proposed Rule Change Concerning Requests for Withdrawal of Certificates by Issuers*, SEC Rel. No. 34-47978, 68 Fed. Reg. 35037, at 35041 (June 4, 2003) (hereafter, the "June 4 SEC Order"). The SEC was empowered to regulate, coordinate, and direct the operations of all persons involved in processing securities transactions; it was directed to "regulate[ ] . . . *every facet* of the securities handling process . . . clearing agencies, depositories, corporate issuers, and transfer agents." Sen. Rep. at 233 (emphasis added).

In developing the new National Clearance and Settlement System, Congress was prescient in foreseeing that "advances in data processing" would

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[6] Petitioners correctly note (Pet. 8 n.4) that following the adoption of Section 17A, the Uniform Commercial Code was revised so that state law of property ownership would recognize that under the new system investors would acquire and transfer "securities entitlements" maintained at "securities intermediaries" rather than paper stock certificates. *See* UCC 8-102(a) (14) & (17), 8-501. The revised UCC also recognized, however, that the SEC-registered clearing agencies (such as respondents) would maintain responsibility for the clearing and settling operations and their rules would be effective even if in conflict with a provision of Article 8. UCC 8-111.

enable the industry to emerge from the ocean of paper in which it was drowning, turning, instead, to electronic systems to evidence ownership and transfer of securities. 15 U.S.C. § 78q-1(a)(1)(C).[7]

2. Pursuant to its delegated authority, the SEC approved the registration of respondents The Depository Trust Company ("DTC") and the National Securities Clearing Corporation ("NSCC") as registered clearing agencies. June 4 SEC Order at 35041; *National Securities Clearing Corp.: Order Granting Registration and Statement of Reasons,* 42 Fed. Reg. 3916 (Jan. 13, 1977).

DTC and NSCC are New York corporations and wholly-owned subsidiaries of respondent The Depository Trust & Clearing Corporation. Each performs separate and critical functions in the federal uniform clearance and settlement system. DTC and NSCC maintain accounts and provide services only for the major financial institutions that constitute their respective participants/members; they do not maintain accounts for issuers or investors, including petitioners here.

DTC is the nation's principal securities depository. It operates an automated, centralized system for book-entry movement of securities positions in the accounts of its participants, the nation's major brokerage houses

[7] The transfer of securities entitlements by electronic means is key to market liquidity. On a daily basis, DTCC's automated systems clear and settle millions of transactions constituting billions of shares of stock. A tiny fraction of today's volumes completely overwhelmed Wall Street during the paperwork crisis.

and banks (who, in turn, serve as securities intermediaries for their own institutional and retail customers). Securities deposited at DTC are registered in the name of DTC's nominee, "Cede & Co.," and immobilized at the depository. This enables DTC to facilitate the automated movements of securities positions without the need to transfer paper indicia of ownership, serving "a critical function in the National Clearance and Settlement System." June 4 SEC Order at 35041 and n.62. Securities on deposit at DTC have a value of over $35 trillion. *See* http://www.dtcc.com/downloads/annuals/2006/2006_report.pdf at p. 30.

NSCC provides centralized clearance, settlement and information services for virtually all broker-to-broker equity, corporate bond and municipal bond and other securities transactions in the United States. As petitioners acknowledge (Pet. 12), in order to facilitate the enormous volume of daily transactions, NSCC's automated "Continuous Net Settlement" system ("CNS") nets down each member-broker's daily position in each security to a single obligation to deliver or receive that security and a corresponding single obligation for payment or receipt of funds. The member-brokers then deliver the net securities or net funds into NSCC's securities settlement system on the settlement date and the system, acting as the central counter-party, allocates the shares and funds to member brokers with a right to receive. *Issuer Restrictions or Prohibitions on Ownership by Securities Intermediaries*, SEC Rel. No. 34-50758, 69 Fed. Reg. 70852 at 70856 and n.55 (Dec. 7, 2004). Changes in beneficial ownership of securities resulting from transactions cleared and settled at NSCC

are implemented by automated book-entry movements of positions in accounts at DTC. June 4 SEC Order at 35014.

The SEC's registration of DTC and NSCC and approval of their rules was necessarily premised on its finding that those agencies, and their rules, met specified statutory objectives implementing the essential objectives of Section 17A, including removing "impediments to and perfect[ing] the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions." 15 U.S.C. § 78q-1(b); *see also* 15 U.S.C. § 78q-1(b)(3)(A) (requiring the SEC to find that clearing agency rules facilitate the prompt and accurate clearance and settlement of securities transactions, safeguard securities).

Clearing agencies such as DTC and NSCC must operate pursuant to their SEC-approved rules, and they cannot issue or alter their rules absent approval by the SEC pursuant to the statutory standards. *See* 17 C.F.R. 240.17a-22; *Depository Trust Co., et al.: Order*, SEC Rel. No. 20221, 48 Fed. Reg. 45167-02, 45171 (Oct. 3, 1983) (approving NSCC and DTC rules); and 15 U.S.C. § 78q-1(a)(2).

3. The SBP was approved by the SEC in 1981 and has been in operation ever since. *See National Securities Clearing Corporation: Proposed Rule Change*, SEC Rel. No. 34-17422, 46 Fed. Reg. 3104 (Jan. 13, 1981) (notice of filing of proposed rule change making SBP permanent), *see also Issuer Restrictions or Prohibitions on Ownership by Securities Intermediaries*, SEC Rel. No. 34-50758, 69 Fed. Reg. 70852, n.57 (Dec. 7, 2004)

("[T]he Stock Borrow Program was approved by the [Securities and Exchange] Commission.").

The SBP is a uniform, automated program used in certain instances where insufficient shares of a particular security have been delivered to NSCC on the settlement date. In order to fulfill its delivery obligations to buying brokers, the CNS system, utilizing the SBP, will automatically borrow securities from members who have (1) voluntarily made such shares available for loan to the clearing corporation and (2) actually have such securities on deposit in their DTC accounts. NSCC then uses these securities, along with the securities delivered to CNS by selling brokers (without making any distinction) to make deliveries to members with the right to receive delivery, thus satisfying the buyer's side of the transaction.

The SBP does not affect the seller's side; a member who has failed to deliver remains obligated to do so. Moreover, sellers who fail to deliver do not and cannot know whether the SBP is being utilized on the settlement date when they failed to deliver. As to the member who has loaned shares through the SBP, those shares are deducted from the member's DTC account (and thus cannot be sold, loaned, pledged, etc. by the lending member until returned to its DTC account).[8]

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[8] Nanopierce's contentions that NSCC has "permit[ted] failures to deliver to remain uncured" and has "facilitated the practice of naked short selling" by market participants (Pet. 14) entirely misapprehends NSCC's role in the National Clearance and Settlement System. NSCC has neither the power nor the obligation to force sellers to deliver; regulatory authority rests

(Cont'd)

4. For all the repeated references to "misrepresentations and omissions," neither Nanopierce's complaint nor its Petition for Certiorari identify any misrepresentations or omissions specific to Nanopierce. The essential claim is that the SBP has undisclosed inherent "defects" (*see* Compl. ¶¶ 89-100) that are alleged to have facilitated the abusive practice of naked short selling and depressed the value of Nanopierce stock (Pet. 14). Reflecting the facial nature of this attack, Nanopierce characterizes the SBP as a "scheme," the "real effect" of which is "to create phantom shares that dilute the value of validly issued shares" (Pet. 15), which respondents fail to disclose to the public.[9]

(Cont'd)
with the SEC and other bodies exercising enforcement powers. *See* www.sec.gov/litigation/briefs/nanopiercesec-brief.pdf at 12-13. To the extent that the gravamen of Nanopierce's claims (as it candidly concedes) is that it and its stockholders have been damaged by "naked short selling" of Nanopierce stock by unscrupulous market participants, its remedies therefore lie either with suits against alleged market manipulators (*see supra* p. 4 and n. 4) or with the SEC and other enforcement authorities. As Nanopierce's own quotation from SEC Chairman Christopher Cox (Pet. 16) suggests, the SEC is exercising its authority to monitor and address the naked short selling issue. *See, e.g.*, Regulation SHO, 17 C.F.R. Part 242.200, and amendments thereto (*Amendments to Regulation SHO*, SEC Rel. 34-56212, 72 Fed. Reg. 45544 (Aug. 14, 2007)).

[9] Nanopierce mischaracterizes its allegations as setting forth a "misuse" of the SBP beyond the purpose for which it is approved (Pet. 14) and as seeking disclosure of DTCC's "actual business practices" (Pet. 19). The complaint, however, is unambiguously premised not on any misuse of the SBP but on the SBP's essential nature (its "real effect") and operation under SEC-approved rules. *See* Pet. App. 31a (no allegation that respondents violate SBP rules).

The affirmative misrepresentation claims are similarly rooted in the SEC-approved rules themselves; petitioners maintain that state law requires DTCC to make disclosures that contradict the rules, despite their federal approval. For example, petitioners allege that the SBP "misrepresents" itself as a borrowing program when it is actually a sale of securities. Compl. ¶ 102 (First Claim for Relief). But the SEC-approved rules explicitly characterize the SBP as a borrowing program. *National Securities Clearing Corporation: Proposed Rule Change*, SEC Rel. No. 34-17422, 46 Fed. Reg. 3104; *see* Pet. App. 19a. Similarly, Nanopierce alleges that the SBP results in the inefficient clearing and settling of trades, and therefore DTCC's public disclosures otherwise (to Congress and the public) are actionable. Compl. ¶ 114 (Second Claim for Relief). But, in approving the SBP rules and continuing to supervise the program, the SEC has already determined that the program meets the Congressional mandate of "remov[ing] impediments to and perfect[ing] the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions." 15 U.S.C. § 78q-1(b)(3)(F); *see also* Pet. App. 20a; www.sec.gov/litigation/briefs/nanopiercesecbrief.pdf at 17-18.[10]

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[10] The remainder of Nanopierce's purported misrepresentation claims (none of which the Petition addresses individually) similarly attack the fundamental nature of the SBP and its rules and are in actuality facial attacks on the program. *See, e.g.*, Compl. ¶¶ 127-130 (Third Claim) (accounting procedures explicitly set forth in the SBP rules (*see* Pet. App. 21a) alleged to "misrepresent" the number of shares in members' accounts); Compl. ¶¶ 139-142 (Fourth Claim) (defendants misrepresent that buy-ins are executed in the marketplace when, allegedly, they

(Cont'd)

The complaint thus challenges the SBP on its face. It seeks to utilize purported state law standards to regulate and ultimately obstruct a federally authorized activity by imposing damage awards on respondents, to the tune of hundreds of millions of dollars, for (1) failing to disclose alleged inherent defects that the SEC did not discern either in approving the program or in its ongoing oversight and (2) making "misrepresentations" that actually constitute the substance of the approved rules.

5. On a motion to dismiss based on federal preemption, lack of personal jurisdiction and failure to state a cause of action, the motion court dismissed Nanopierce's suit under the preemption doctrine, without reaching the other grounds asserted. Pet. App. 28a at 31a-32a. The Nevada Supreme Court affirmed, holding that Nanopierce's claims

> conflict with Congress's regulatory scheme, since imposing the requirements implicated by appellants' state law claims, which they primarily base on allegations that respondents conceal flaws in a Commission-approved national system for clearing and settling securities transaction, frustrates Congress's

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(Cont'd)
are executed through the SBP, even though the rules (cited in Compl. ¶ 91) explicitly state that buy-ins are executed in the marketplace). *See* Pet App. 17a-21a (finding by the court below that each SBP "misrepresentation" claim asserted here actually constitutes challenge to the program as approved and is preempted); *Pet Quarters*, 2008 U.S. Dist. LEXIS 15316, at * 15-18 (same).

> objectives with respect to the clearing and settling regulatory scheme and renders adherence to both that regulatory scheme and state law impossible.

Pet. App. 24a.

REASONS FOR DENYING THE PETITION

I. THERE IS NO CONFLICT BETWEEN THE NEVADA SUPREME COURT'S DECISION AND THE INAPPOSITE AUTHORITIES CITED BY PETITIONERS

There is no conflict between the decision below and any decision of any court of appeal or state high court, notwithstanding strained contentions to the contrary. The Nevada Supreme Court's holding is in line with all the other decisions addressing conflicts preemption in comparable cases, and presents no issue warranting this Court's review.

Nanopierce seeks to have a state court jury find that the SBP has "defects" that the SEC has determined do not exist, and award enormous damages against respondents for failing to make disclosures of these inherent "defects" and other matters that conflict with the SEC-approved SBP rules. This application of state law, as erroneously construed by Nanopierce, stands as an obstacle to Congress' determination that the SEC would exercise plenary authority over "every facet" of a uniform system for clearing and settling the nation's securities transactions – here manifested by the approval of the SBP – requiring preemption of those state claims

under longstanding authority. *See Geier v. American Honda Motor Co.*, 529 U.S. 861, 881-82 (2000); *Fid. Fed. Sav. & Loan Ass'n v. de la Cuesta*, 458 U.S. 141, 155 (1982) (where federal agency permitted, but did not mandate, banks to enforce due-on-sale clauses in their mortgages, state law prohibiting such clauses was barred under conflicts preemption); *see also Credit Suisse First Boston Corp v. Grunwald*, 400 F.3d 1119, 1128 (9th Cir. 2005) (SRO rules approved by the SEC preempt conflicting state law), *citing Merrill Lynch, Pierce, Fenner & Smith v. Ware*, 414 U.S. 117, 127 (1973).[11]

1. The Delaware Supreme Court's decision in *O'Malley v. Boris*, 742 A.2d 845 (Del. 1999), the centerpiece of Nanopierce's argument (Pet. 20-22), presents no conflict with the decision below. *O'Malley* was a suit by customers against their broker for its fraudulent misrepresentations concerning their own accounts – wholly unlike the present suit against self-regulatory organizations (that have no interactions with the petitioners) responsible for operating the national clearance and settlement system under SEC-approved

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[11] *Geier* found that the plaintiffs' state law claims were barred by conflicts preemption notwithstanding a "savings clause," in the federal statute, as courts have done regularly. *Id.*, 529 U.S. at 870 (citing cases); *see also, e.g., Int'l Paper Co. v. Ouellette*, 479 U.S. 481, 497 (1987) (finding conflicts preemption of state law claims notwithstanding a savings clause in the Clean Water Act); *American Agricultural Movement, Inc, v. Board of Trade of Chicago*, 977 F.2d 1147, 1155 (7th Cir. 1992) (finding conflicts preemption notwithstanding savings clause in Commodity Exchange Act). Petitioners' discussion of various savings clauses (Pet. 9-10) has no bearing on the conflicts preemption analysis.

rules. In *O'Malley*, the brokerage firm utilized a "negative response" letter pursuant to an NASD rule to notify its customers of an intent to transfer their accounts, without disclosing that the brokerage firm would benefit financially by doing so. The defense that the claims were preempted was unavailing because disclosing the broker's financial interest in transferring the accounts "would not interfere with the purpose of effectiveness of the NASD rule. . . ." 742 A.2d at 849. Here, by stark contrast, the requested disclosures flatly contradict the fact of the SEC's approval as well as the actual language of the SBP. Nor is *O'Malley* otherwise analogous to petitioners' claims here. The analogous claim would be a damages action under state law against brokers who failed to disclose that the NASD-approved "negative response" program inherently operated as a fraud against their customers. Nothing in *O'Malley* remotely indicates that the Delaware Supreme Court would have permitted such claim. *Compare O'Malley*, 742 A.2d at 849.

That *O'Malley* poses no conflict whatever is plain from the Delaware Supreme Court's express distinction of its decision from *Guice v. Charles Schwab & Co.*, 674 N.E.2d 282 (N.Y. 1996) *cert. denied*, 520 U.S. 1118 (1997), which the Petition acknowledges is consistent with the Nevada Supreme Court's decision here. (Pet. 22.) The New York Court of Appeals in *Guice* held that state law claims based on allegedly inadequate disclosures concerning order flow payments were preempted in light of the SEC's specific requirements regarding what had to be disclosed. *Guice*, 674 N.E.2d at 288. By contrast, the NASD rule at issue in *O'Malley* did not purport to limit the disclosures which may be included in a "negative action" letter. *O'Malley*, 742 A.2d at 849.

2. Nanopierce's attempt to create a decisional conflict with cases involving the Federal Alcohol Administration Act and the Federal Insecticide, Fungicide and Rodenticide Act ("FIFRA") (Pet. 23-30) is bootless. *Bates v. Dow Agrosciences LLC*, 544 U.S. 431 (2005) and *Bronco Wine Co. v. Jolly*, 95 P.3d 422 (Cal. 2004), *cert. denied*, 546 U.S. 1150 (2006), were express preemption cases in which the courts construed Congress's intent in adopting the precise preemption language at issue. The holdings of non-preemption were premised in significant part on the facts that the federal statutes at issue contemplated supplemental state regulation. In fact, FIFRA was held to be a "decentralized" statutory scheme which permitted states to ban pesticides that the EPA had approved. *Bates*, 544 U.S. at 451; *see also Bronco Wine*, 95 P.3d at 447-450. Here, by stark contrast, Congress mandated "*uniform standards and procedures for clearance and settlement*" under SEC-approved rules. 15 U.S.C. 78q-1(a)(1)(D) (emphasis added).

3. The Petition also ignores both the companion SBP cases (*supra*, n.1) and *American Agricultural Movement, Inc, v. Board of Trade of Chicago, supra* (hereafter, "*AAM*"), where the Seventh Circuit held preempted state law claims asserted against the Chicago Board of Trade – notwithstanding a savings clause in the pertinent federal regulation – because permitting the plaintiff to bring its state law claims against the Board of Trade would frustrate Congress' intent to bring the markets under a uniform set of regulations.

In *AAM*, plaintiffs had asserted various Illinois common law claims against a program operated by the

Chicago Board of Trade, pursuant to the authority of the federal Commodities Exchange Act. In holding those claims to be preempted, the Seventh Circuit held that preemption was not mandated where resolution of a dispute would affect only the relationship between broker and investor – both marketplace participants involved in the purchase and sale of securities – but would apply where the proposed application of state law would directly affect the operations of the Board of Trade itself. *Id.* 977 F.2d at 1156-57. As the court explained:

> [A] law of general application, when applied in a manner that would govern or supervise the operation of or trading on a contract market, raises the same unwelcome specter of non-uniformity as does a law that, by its terms, purports to govern or supervise the same. The crucial inquiry, we reiterate, is the context in which a law is applied . . . . Laws of general application of course operate in a variety of arenas, and are preempted only when [Appellants] attempt to use them in a manner that would, in effect, regulate the futures markets.

Id. at 1157. Here, as in *AAM*, Congress has set national uniformity as a central goal in operating the post-trade securities handling process, and claims asserted under state laws of general application are preempted to the extent that litigants seek to apply them so as to interfere with the uniform federal policy.

Nor may Nanopierce escape preemption by arguing (as it did in the Nevada courts) that its Complaint seeks

only damages, and not injunctive relief dismantling the SBP. It is beyond dispute that "a liability award 'can be, indeed is designed to be, a potent, method of governing conduct and controlling policy.'" *Riegel v. Medtronic, Inc.*, 128 S. Ct. 999, 1008 (2008), *citing Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 521 (1992). Since it is the SEC, and not the state courts, that is vested by Congress with determining whether DTCC's programs are accurate and efficient and otherwise meet the standards required by Section 17A, the judgment below is correct and warrants no further review. Once the SEC has so determined with regard to DTCC's necessarily uniform system, it would undermine Congress's expressed goals to permit the courts of the 50 states to revisit and overrule that determination, whether by injunction or by the imposition of damages awards.

II. THE DECISION RAISES NO IMPORTANT ISSUE WARRANTING THIS COURT'S REVIEW

Contrary to the Petition's claims, the decision below has no implications whatever concerning the interplay of federal and state policies of full and fair disclosure to investors and the remedies available to investors. It concerns not misrepresentations or omissions made by brokers to customers, or by anyone in connection with the purchase or sale of securities in the marketplace, but whether the operation of the system mandated by Congress and overseen by the SEC for post-trade clearing and settlement can be subject to purported state law disclosure obligations that contradict, and therefore obstruct, the federally approved system. Petitioners' discussion of state regulation of securities trading (Pet. 4-6) ignores the distinction between regulation of

trading; *i.e.*, disclosures in connection with the purchase and sale of securities, and regulation of the uniform clearance and settlement system. As petitioners concede, respondents' systems only come into play *after* the trading decisions have been made (Pet. 2), and thus petitioners' discussion of state remedies "for investors harmed by misrepresentation" strays far from the mark. *Cf. AAM*, 977 F.2d at 1156-57.

III. THERE IS NO NEED TO HOLD THE PETITION PENDING THIS COURT'S DECISION IN *ALTRIA*, WHICH RAISES WHOLLY SEPARATE ISSUES

Finally, there is no need for this Court to hold the present Petition pending its review of *Altria Group, Inc. v. Good*, 128 S. Ct. 1119 (2008) (*cert. granted* Jan. 16, 2008), an inapposite case involving the preemptive scope of the express federal preemption provision in federal tobacco regulations in the context of false advertising claims. The statute at issue in *Altria*, the Federal Cigarette Labeling and Advertising Act, 15 U.S.C. § 1334(b), expressly precludes states from imposing requirements with respect to cigarette advertising "based on smoking or health" and the issue to be decided on *certiorari* is whether the express preemption provision precludes the application of state law unfair trade practices claim alleging a cigarette ad to be deceptive. There is no reason to suppose that in *Altria* this Court will address implied preemption in a context pertinent to this case, and *Altria* contains nothing like the statutory provision here directing the establishment

of a system with national uniformity. *Altria* is unlikely to provide additional guidance applicable to Nanopierce's preempted facial attack, and the Petition should be denied forthwith.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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APPENDIX

APPENDIX — AMENDED COMPLAINT OF THE SECOND JUDICIAL DISTRICT COURT FOR THE COUNTY OF WASHOE, STATE OF NEVADA DATED MAY 11, 2004

SECOND JUDICIAL DISTRICT COURT
COUNTY OF WASHOE, STATE OF NEVADA

CASE NO. CV04-01079

DEPT. NO. 4

NANOPIERCE TECHNOLOGIES, INC., A NEVADA CORPORATION; STEPHEN SEITZ, AN INDIVIDUAL; JANE SEITZ, AN INDIVIDUAL, KATHY KNIGHT-MCCONNELL, AN INDIVIDUAL, JAMES STOCK, AN INDIVIDUAL, MAUREEN O'SULLIVAN, AN INDIVIDUAL, AND HELEN KOLADA, AN INDIVIDUAL

Plaintiffs,

-against-

THE DEPOSITORY TRUST AND CLEARING CORPORATION; THE DEPOSITORY TRUST COMPANY; AND THE NATIONAL SECURITIES CLEARING CORPORATION,

Defendants.

AMENDED COMPLAINT

BUSINESS COURT REQUESTED

REQUEST EXEMPTION FROM ARBITRATION

Appendix

Plaintiff Nanopierce Technologies, Inc. ("Nanopierce"), Plaintiff Stephen Seitz and Plaintiff Jane Seitz (together, "Seitz"), Plaintiff Kathy Knight-McConnell ("Knight-McConnell"), Plaintiff James Stock ("Stock"), Plaintiff Maureen O'Sullivan ("O'Sullivan") and Plaintiff Helen Kolada ("Kolada") (collectively, the "Plaintiffs") for their complaint against Defendant Depository Trust and Clearing Corporation ("DTCC") and its subsidiaries, Defendant Depository Trust Company ("Depository Trust"), and Defendant National Securities Clearing Corporation ("NSCC") (collectively, the "Defendants"), allege and set forth as follows:

I. Summary

1. The Stock Borrow Program (as described below, commencing at paragraph 84) was purportedly created to address SHORT TERM delivery failures by sellers of securities in the stock market. However, the end result of the program has been to create tens of millions of unissued and unregistered shares to be traded in the public market. Further, in some instances, the Stock Borrow Program has resulted in two or more shareholders who purchase shares in separate transactions to own the same shares.

In the securities marketplace, sellers advertise asking prices and buyers advertise offering prices. When the two prices match, a trade occurs. Clearance is the process of verifying and confirming the terms of the trade, such as the number of shares, price, buyer and seller. After a trade clears, it settles on the date prescribed by

regulation, which means that the seller delivers the shares and the buyer delivers payment. Sometimes the seller is unable to deliver the shares at settlement. When shares are not delivered on settlement day (the "Settlement Day"), the seller is said to have "failed to deliver" the shares. This event is referred to in the securities industry as a "fail to deliver".

Prior to 1981, when a fail to deliver occurred, the buyer held back his payment and waited for the seller to deliver the shares. If the buyer got tired of waiting for the seller to deliver the shares, the buyer went into the market and bought the shares from another seller. This process of going back to the market to buy shares to replace the ones which were not delivered is called "buying in" or a "buy-in." If the price of the shares increased between the time that the buyer originally bought the shares and the time the buyer went into the market to replace them, the buyer charged the additional cost to the seller who failed to deliver. Until 1981, there were only two alternatives available to a buyer whose seller failed to deliver: either wait for the shares to be delivered or go back into the market and buy in the shares.

In an effort to streamline the back office operations of the securities industry, the clearance and settlement functions for virtually all securities trades in the United States were consolidated in the Depository Trust and the NSCC. In 1981, the NSCC created the Stock Borrow Program, purportedly to improve the efficiency of the clearance and settlement function by addressing temporary fail to deliver situations. Under the Stock

Borrow Program, if a seller fails to deliver the shares on time, the NSCC borrows the shares from willing lenders[1] and gives the shares to the buyer in settlement of the trade. The Stock Borrow Program operates through a computer process and now represents the only way that a buyer can cure a fail to deliver by a seller. However, in reality, the Stock Borrow Program does not cure the fail to deliver. The seller still owns the shares. The only change is that the party waiting for the shares is no longer the buyer. Now, it is the NSCC.

Since the NSCC instituted the Stock Borrow Program, there is little incentive for the NSCC to require sellers to cure fail to deliver positions once the loan has been made. The Stock Borrow Program has become a reliable source of income for the Depository Trust, the NSCC and willing lenders who have shares on deposit at the Depository Trust. For the year ended December 31, 2003, the Depository Trust reported revenues from services of $425,416,000 and the NSCC reported revenues from services of $293,133,000.

"The failure of participants to deliver securities to NSCC on settlement date, and the corresponding failure of NSCC to redeliver the securities, results in open positions. . . . At the close of business on December 31, 2003, open positions due to NSCC approximated $3,025,467,000 . . . , and open positions due by NSCC to

1. Willing lenders are brokers and clearing firms who lend their customers' shares to the NSCC. These shares are ultimately held at the Depository Trust through a chain of custody that begins with the customers delivering share certificates to brokers who then deliver the certificates to the Depository Trust.

participants approximated $2,303,717,000 ... for unsettled positions and $721,750,000 ... for securities borrowed through the NSCC's Stock Borrow Program."[2] Because these open positions represent shares borrowed by the NSCC and given to buyers, the NSCC has subjected itself to the risk of significant financial loss if the sellers who failed to deliver are unable to honor their obligation to deliver the shares. In an attempt to reduce this exposure, the Defendants have participated in a scheme to manipulate downward the price of the affected securities, thereby reducing the market value of the open fail to deliver positions with respect to these affected securities. Consequently, fails to deliver, particularly in trades of small capitalization companies such as Plaintiff Nanopierce, are no longer temporary, and frequently remain uncured for months and even years.

The Defendants have permitted sellers to maintain open fail to deliver positions of tens of millions of shares for periods of a year and even longer. This course of conduct by the Defendants has had the effect of creating millions of unregistered illegal free trading shares of the issuer, artificially (1) increasing the supply of an issuer's shares in the marketplace; (2) driving down the price of the stock of the issuer; (3) decreasing the value of the shareholders' holdings in an issuer's stock; and (4) causing multiple owners who purchased shares in separate transactions to own the same shares. Neither the Depository Trust nor the NSCC has authority to

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2. National Securities Clearing Corporation Annual Financial Statements (2003).

issue or create shares. Only the issuer (Plaintiff Nanopierce) has authority to do so.

The abuses of the Stock Borrow Program have been recognized by the National Association of Securities Dealers ("NASD") and measures have been proposed to address them. "Concerns have been raised by members, issuers, investors and other interested parties about potentially abusive short selling activities occurring in the marketplace. In particular, naked short selling, or selling short without borrowing securities to make delivery, *can result in long term failures to deliver, including aggregate failures to deliver that exceed the total float of a security. NASD believes such extended failures to deliver can have a negative effect on the market. Among other things, by not having to deliver securities, naked short sellers can take on larger short positions than would otherwise be permissible, which can facilitate manipulative activity.*"[3]

II. Parties, Jurisdiction, and Venue

2. Plaintiff Nanopierce is a Nevada corporation, with its principal place of business in Denver, Colorado.

3. Plaintiff Seitz are individual shareholders of Nanopierce who reside at Otego, New York.

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3. NASD Proposed Amendments Relating to Short Sale Delivery Requirements (SR-NASD-2004-044) (emphasis added).

4. Plaintiff Knight-McConnell is an individual shareholder of Nanopierce who resides at Bronx, New York.

5. Plaintiff Stock is an individual shareholder of Nanopierce who resides at Henderson, Nevada.

6. Plaintiff O'Sullivan is an individual shareholder of Nanopierce who resides at Cleveland, Ohio.

7. Plaintiff Kolada is an individual shareholder of Nanopierce who resides at Cleveland, Ohio.

8. Defendant DTCC is a New York corporation and may be served at its principal place of business at 55 Water Street, New York, New York 10041-0099, Attention: General Counsel.

9. Defendant NSCC is a New York corporation and may be served at its principal place of business at 55 Water Street, New York, New York 10041-0099, Attention: General Counsel.

10. Defendant Depository Trust is a limited purpose trust company formed under the Banking laws of New York and may be served at 55 Water Street, New York, New York 10041-0099, Attention: General Counsel.

11. This Court has subject matter jurisdiction.

12. This Court has personal jurisdiction over the Defendants.

13. Venue is lodged in this Court pursuant to NRS 13.040.

III. General Allegations

A. Plaintiff Nanopierce

14. Shares of Nanopierce are traded on the NASDAQ Over the Counter Bulletin Board under the symbol "NPCT.OB". These shares are eligible to be held in book-entry form at the Depository Trust. According to its Articles of Incorporation and amendments thereto filed with the Nevada Secretary of State, Nanopierce is authorized to issue 200,000,000 shares of common stock.

15. On or about October 20, 2000, Nanopierce entered into a $15,000,000 Purchase Agreement ("Purchase Agreement") with Harvest Court LLC ("Harvest Court") to sell Nanopierce common stock in two installments.

16. At the first closing on October 20, 2000 (the "First Closing"), Nanopierce sold 4,531,161 shares of its common stock to Harvest Court along with a common stock purchase warrant of 453,161 shares. The number of shares Nanopierce sold pursuant to the Purchase Agreement was determined by a formula based on the average closing bid price of Nanopierce stock for ten consecutive trading days before the First Closing.

17. The Purchase Agreement also contained a reset provision which required that Nanopierce issue additional shares to Harvest Court on three separate dates following the First Closing. The number of shares to be issued pursuant to the reset provision was determined by a formula based on the average of the twenty-two lowest closing bid prices of Nanopierce stock during the sixty-five trading days immediately preceding the applicable reset issuance dates.

18. Pursuant to the reset provision in the Purchase Agreement, Nanopierce issued an additional 2,143,975 shares of its common stock to Harvest Court on or about January 31, 2001.

19. After the First Closing, the price of Nanopierce common stock declined continuously from $2.56 on October 20, 2000 to $0.31 on April 23, 2004.

20. Upon information and belief, during the period between the First Closing and April 23, 2004, Nanopierce stock was actively traded and these trades were cleared and settled by the Defendants.

21. Upon information and belief, the price of Nanopierce stock fell because the operation of the Stock Borrow Program by Defendants allowed the manipulation of Nanopierce stock by various sellers who failed to deliver Nanopierce shares.

22. The Defendants permitted sellers to maintain significant open fail to deliver positions of millions of

shares of Nanopierce stock for extended periods of time by implementing the Stock Borrow Program to cover these open positions.

23. By covering open fail to deliver positions with shares borrowed through the Stock Borrow Program and delivering the borrowed shares to the buyers, the Defendants artificially created unregistered, free trading Nanopierce shares and increased the supply of Nanopierce shares in the marketplace without authority.

24. The artificially increased supply of Nanopierce shares in the marketplace created by Defendants' borrowing of Nanopierce shares through the Stock Borrow Program caused a dramatic devaluation of Nanopierce stock. As a result, Nanopierce is damaged in an amount to be proven at trial.

B. Plaintiffs Seitz

25. Plaintiffs Seitz are individual shareholders of Nanopierce.

26. During the period between March 2000 and March 2004, Plaintiffs Seitz purchased and sold Nanopierce shares at various pricing ranging from a high of $6.06 to a low of $0.148.

27. Upon information and belief, when Plaintiffs Seitz purchased and sold Nanopierce shares, these transactions were cleared and settled by the Defendants.

Appendix

28. Upon information and belief, the Defendants borrowed Plaintiffs Seitz' Nanopierce shares through the Stock Borrow Program to cover open fail to deliver positins in Nanopierce stock created by sellers who failed to deliver by Settlement Day.

29. Upon information and belief, the price of Nanopierce stock fell because the Defendants' operation of the Stock Borrow Program facilitated or permitted the manipulation of Nanopierce stock by various sellers who failed to deliver Nanopierce shares by Settlement Day.

30. The Defendants permitted certain sellers to maintain significant open fail to deliver positions of millions of shares of Nanopierce stock for extended periods of time well beyond Settlement Day by implementing the Stock Borrow Program to cover these open positions.

31. By covering open fail to deliver positions with shares borrowed through the Stock Borrow Program and delivering the borrowed shares to the buyers, the Defendants have artificially created unregistered, free trading Nanopierce shares and increased the supply of Nanopierce shares in the marketplace without authority.

32. The artificially increased supply of Nanopierce shares in the marketplace created by Defendants' borrowing of Nanopierce shares through the Stock Borrow Program has significantly decreased the value of Nanopierce stock and Plaintiffs Seitz' holding in Nanopierce stock. As a result, Plaintiffs Seitz are damaged in an amount to be proven at trial.

C. Plaintiff Knight-McConnell

33. Plaintiff Knight-McConnell is an individual shareholder of Nanopierce.

34. During the period between January 2001 and March 2004, Plaintiff Knight-McConnell purchased and sold Nanopierce shares at various prices ranging from a high of $1.64 to a low of $0.15.

35. Upon information and belief, when Plaintiff Knight-McConnell purchased and sold Nanopierce shares, these transactions were cleared and settled by the Defendants.

36. Upon information and belief, the Defendants borrowed Plaintiff Knight-McConnell's Nanopierce shares through the Stock Borrow Program to cover open fail to deliver positions in Nanopierce stock created by sellers who failed to deliver by Settlement Day.

37. Upon information and belief, the price of Nanopierce stock fell because the Defendants' operation of the Stock Borrow Program facilitated or permitted the manipulation of Nanopierce stock by various sellers who failed to deliver Nanopierce shares by Settlement Day.

38. The Defendants permitted certain sellers to maintain significant open fail to deliver positions of millions of shares of Nanopierce stock for extended periods of time well beyond Settlement Day by implementing the Stock Borrow Program to cover these open positions.

39. By covering open fail to deliver positions with shares borrowed through the Stock Borrow Program and delivering the borrowed shares to the buyers, the Defendants have artificially created unregistered, free trading Nanopierce shares and increased the supply of Nanopierce shares in the marketplace without authority.

40. The artificially increased supply of Nanopierce shares in the marketplace created by Defendants' borrowing of Nanopierce shares through the Stock Borrow Program has significantly decreased the value of Nanopierce stock and Plaintiff Knight-McConnell's holding in Nanopierce stock. As a result, Plaintiff Knight-McConnell is damaged in an amount to be proven at trial.

D. Plaintiff Stock

41. Plaintiff Stock is an individual shareholder of Nanopierce.

42. During the period between March 2002 and March 2004, Plaintiff Stock purchased and sold Nanopierce shares at various prices ranging from a high of $1.00 to a low of $0.16.

43. Upon information and belief, when Plaintiff Stock purchased and sold Nanopierce shares, these transactions were cleared and settled by the Defendants.

44. Upon information and belief, the Defendants borrowed Plaintiff Stock's Nanopierce shares through

the Stock Borrow Program to cover open fail to deliver positions in Nanopierce stock created by sellers who failed to deliver by Settlement Day.

45. Upon information and belief, the price of Nanopierce stock fell because the Defendants' operation of the Stock Borrow Program facilitated or permitted the manipulation of Nanopierce stock by various sellers who failed to deliver Nanopierce shares by Settlement Day.

46. The Defendants permitted certain sellers to maintain significant open fail to deliver positions of millions of shares of Nanopierce stock for extended periods of time well beyond Settlement Day by implementing the Stock Borrow Program to cover these open positions.

47. By covering open fail to deliver positions with shares borrowed through the Stock Borrow Program and delivering the borrowed shares to the buyers, the Defendants have artificially created unregistered, free trading Nanopierce shares and increased the supply of Nanopierce shares in the marketplace without authority.

48. The artificially increased supply of Nanopierce shares in the marketplace created by Defendants' borrowing of Nanopierce shares through the Stock Borrow Program has significantly decreased the value of Nanopierce stock and Plaintiff Stock's holding in Nanopierce stock. As a result, Plaintiff Stock is damaged in an amount to be proven at trial.

E. Plaintiff O'Sullivan

49. Plaintiff O'Sullivan is an individual shareholder of Nanopierce.

50. During the period between June 2000 and March 2004, Plaintiff O'Sullivan purchased and sold Nanopierce shares at various prices ranging from a high of $2.0937 to a low of $.34.

51. Upon information and belief, when Plaintiff O'Sullivan purchased and sold Nanopierce shares, these transactions were cleared and settled by the Defendants.

52. Upon information and belief, the Defendants borrowed Plaintiff O'Sullivan's Nanopierce shares through the Stock Borrow Program to cover open fail to deliver positions in Nanopierce stock created by sellers who failed to deliver by Settlement Day.

53. Upon information and belief, the price of Nanopierce stock fell because the Defendants' operation of the Stock Borrow Program facilitated or permitted the manipulation of Nanopierce stock by various sellers who failed to deliver Nanopierce shares by Settlement Day.

54. The Defendants permitted certain sellers to maintain significant open fail to deliver positions of millions of shares of Nanopierce stock for extended periods of time well beyond Settlement Day by implementing the Stock Borrow Program to cover these open positions.

55. By covering open fail to deliver positions with shares borrowed through the Stock Borrow Program and delivering the borrowed shares to the buyers, the Defendants have artificially created unregistered, free trading Nanopierce shares and increased the supply of Nanopierce shares in the marketplace without authority.

56. The artificially increased supply of Nanopierce shares in the marketplace created by Defendants' borrowing of Nanopierce shares through the Stock Borrow Program has significantly decreased the value of Nanopierce stock and Plaintiff O'Sullivan's holding in Nanopierce stock. As a result, Plaintiff O'Sullivan is damaged in an amount to be proven at trial.

F. Plaintiff Kolada

57. Plaintiff Kolada is an individual shareholder of Nanopierce.

58. During the period between July 2001 and October 2003, Plaintiff Kolada purchased and sold Nanopierce shares at various prices ranging from a high of $1.70 to a low of $.21.

59. Upon information and belief, when Plaintiff Kolada purchased and sold Nanopierce shares, these transactions were cleared and settled by the Defendants.

60. Upon information and belief, the Defendants borrowed Plaintiff Kolada's Nanopierce shares through

the Stock Borrow Program to cover open fail to deliver positions in Nanopierce stock created by sellers who failed to deliver by Settlement Day.

61. Upon information and belief, the price of Nanopierce stock fell because the Defendants' operation of the Stock Borrow Program facilitated or permitted the manipulation of Nanopierce stock by various sellers who failed to deliver Nanopierce shares by Settlement Day.

62. The Defendants permitted certain sellers to maintain significant open fail to deliver positions of millions of shares of Nanopierce stock for extended periods of time well beyond Settlement Day by implementing the Stock Borrow Program to cover these open positions.

63. By covering open fail to deliver positions with shares borrowed through the Stock Borrow Program and delivering the borrowed shares to the buyers, the Defendants have artificially created unregistered, free trading Nanopierce shares and increased the supply of Nanopierce shares in the marketplace without authority.

64. The artificially increased supply of Nanopierce shares in the marketplace created by Defendants' borrowing of Nanopierce shares through the Stock Borrow Program has significantly decreased the value of Nanopierce stock and Plaintiff Kolada's holding in Nanopierce stock. As a result, Plaintiff Kolada is damaged in an amount to be proven at trial.

G. DTCC

65. DTCC is a holding company which consists of four subsidiaries (one depository and three clearing corporations): the Depository Trust, the NSCC, the Fixed Income Clearing Corporation and the Emerging Markets Clearing Corporation.

66. DTCC, through its subsidiaries, provides clearance, settlement and information services for equities, corporate and municipal bonds, government and mortgage backed securities, over-the-counter credit derivatives and emerging market debt trades.

67. In 2003, the value of securities cleared and settled through the DTCC was stated to be $923.4 trillion. The DTCC's total revenue for 2003 was stated to be $947 million.

68. Upon information and belief, the DTCC, through its subsidiaries provides its services to Nevada corporations and residents.

H. Depository Trust

69. Depository Trust is a subsidiary of the DTCC. It is the world's largest securities depository and a clearinghouse for settlement of securities trading activity.

70. Depository Trust was formed 30 years ago to eliminate the physical movement of securities among brokerage firms on Wall Street to satisfy delivery requirements.

71. Financial organizations deliver securities on behalf of their customers through computerized bookkeeping records (also known as book-entry deliveries) at the Depository Trust without ever physically transferring the securities. In 2003, the value of book-entry deliveries processed by the Depository Trust was stated to be $105.7 trillion.

72. Depository Trust records the transfer of securities by book-entry by debiting the transferor's Depository Trust account and crediting the transferee's Depository Trust account.

73. Depository Trust also retains physical custody of stock certificates on behalf of its members. Stock certificates for registered securities deposited with the Depository Trust are held in the name of Cede & Co., Depository Trust's nominee name. As of December 31, 2003, the value of securities on deposit at the Depository Trust was stated to be $24.6 trillion and the number of depository-eligible securities was stated to be 2,227,000.

74. Upon information and belief, the Depository Trust provides its services to Nevada corporations and residents.

Appendix

I. NSCC

75. NSCC was created in 1976 as a result of the merger of three major clearing corporations (NYSE, AMEX, and NASD). In 2003, the total number of transactions processed by the NSCC was stated to be 4.7 billion with a value of $81.2 trillion.

76. NSCC, in conjunction with the Depository Trust, provides centralized clearance, settlement and information services for virtually all broker-to-broker equity, corporate bond and municipal bond, exchange-traded funds and unit investment trust trades that occur in the United States.

77. Upon information and belief, the NSCC provides its services to Nevada corporations and residents.

J. Continuous Net Settlement System

78. Transactions processed by the NSCC clear and settle through the Continuous Net Settlement System ("CNS System"). Sellers and buyers who clear and settle through the CNS System are required to be members of the NSCC and the Depository Trust ("Members").

79. NSCC guarantees completion of the transactions it processes through the CNS System by assuming (i) the obligation of the buyers to make payment to the sellers upon delivery of the shares, and (ii) the obligation of the sellers to deliver shares to the buyers.

Appendix

80. Each day during the daytime allocation cycle, the CNS System continually nets all trades of its Members by security to net long (purchase) and net short (sale) positions which are then further netted with closing positions carried forward from the previous trading day. The resulting net positions represent the quantity of each security due for settlement by the Members. A long position represents the quantity owed to the Members by the NSCC and a short position represents the quantity owed to the NSCC by the Members. After determination of a Member's long and short positions at the end of the daytime allocation cycle, the positions are passed to the Depository Trust for processing over the evening allocation cycle.

81. The short positions are compared to the Member's Depository Trust account to determine if the number of shares on deposit is sufficient to settle the short positions. If so, the shares are transferred from the Member's Depository Trust account to the NSCC's Depository Trust account. Shares received from Members in settlement of short positions are placed in the NSCC's Depository Trust account awaiting instructions from NSCC for delivery to the Depository Trust accounts of Members in long positions.

82. Based on instructions from the NSCC, as shares are received by the NSCC from Members with short positions, they are automatically allocated from the NSCC's Depository Trust accounts to the Depository Trust accounts of Members with long positions.

83. Early morning on the next business day, after regular evening allocation processing, the NSCC determines which open short positions are high-priority obligations. The NSCC then attempts to borrow shares through the Stock Borrow Program to satisfy these open positions.

K. Stock Borrow Program

84. The Stock Borrow Program allows the, NSCC to borrow available stocks from participating Members to cover short positions that remain open after a day's trade. These short positions are created by priority requests for allocation, buy-ins submitted by Members, the need to deliver against omnibus positions with other clearing corporations and by sellers' fails to deliver.

85. As provided in Addendum C-1 of the Rules and Procedures of the National Securities Clearing Corporation, (effective December 26, 2003), the process of the Stock Borrow Program is as follows:

(a) On a daily basis, Members who wish to participate in the Stock Borrow Program inform NSCC of the number of shares of each security that are available to be borrowed in their general unpledged account at the Depository Trust.

(b) Each morning, after the evening allocation cycle, the NSCC determines which short positions still remain open.

(c) If a short position remains open, the NSCC attempts to borrow securities from its Members to satisfy these open positions.

(d) The NSCC uses a formula to determine the order in which it will borrow securities from its Members and utilizes the full amount of shares available from one Member before borrowing from the next Member in sequence.

(e) When the shares are borrowed, the lending Member's Depository Trust account is debited by the number of borrowed shares. The borrowed shares are then credited to the NSCC's Depository Trust account and transferred to the buyer's Depository Trust account. The buyer acquires all right, title and interest in the borrowed shares, including the right to vote, receive dividends and resell the shares, without encumbrance or any reservation of rights.[4]

(f) The NSCC records the borrowing of the shares as a long position in a special CNS sub-account set up specifically for the lending Member's stock borrow activity.

(g) The NSCC credits the lending Member's regular CNS account with funds equivalent to the total current

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4. As noted in NASD Proposed Amendments Relating to Short Sale Delivery Requirements (SR-NASD-2004-044), "significant failures to deliver can impact certain rights of buyers, such as the right to vote shares or the treatment of dividends".

market value of the borrowed shares which the lending Member may invest to earn interest overnight.

(h) The NSCC also receives a fee from the Member who created the short position requiring the NSCC to borrow the shares through the Stock Borrow Program.

86. Shares borrowed by the NSCC are only returned when regular short deliveries from sellers for that day exceed priority needs in a particular security.

87. Through normal allocation to the CNS sub-account of the lending Members, borrowed shares which are returned are allocated to the lending Members' accounts at current market prices and the returned shares are transferred from the NSCC's Depository Trust account to the lending Member's Depository Trust account. The NSCC distributes reports to the lending Members each morning, reflecting stock borrow activity.

88. Membership in both the NSCC and Depository Trust is required in order to be a lender in the Stock Borrow Program. Lenders are selected based on a certain formula. Each day the lending Members are assigned a random allocation number for each security made available. A factor is developed for each lending Member by dividing the percentage of each lending Member's average loans as they relate to total NSCC borrowings by the percentage of each lending Member's average fees paid for trade comparison, trade recording and clearance as they relate to the total fees for all Members. Each random allocation number is then multiplied by

the factor to produce an adjusted random number per position for each lending Member. The lending Member with the lowest number will receive the first priority for borrowing.

L. The Dilutive Effects of the Stock Borrow Program

89. One of the effects of the Stock Borrow Program is to allow sellers to continue to fail to deliver because the NSCC can borrow shares from the Stock Borrow Program to cover the fail to deliver positions.

90. If the seller fails to deliver the sold shares on Settlement Day, a short position for that seller is created in the CNS System which is ultimately covered by the Stock Borrow Program either directly through the NSCC's daily allocation cycle or indirectly through a buy-in executed with shares borrowed through the Stock Borrow Program.

91. In the case of a buy-in, as set forth in the Rules and Procedures of the National Securities Clearing Corporation (effective December 26, 2003), when a seller fails to deliver, the buyer notifies the NSCC that it intends to buy-in the seller's fail to deliver position. However, instead of executing the buy-in by going into the market, the NSCC executes the buy-in by borrowing shares from lending Members of the Stock Borrow Program.

92. As a result, the Stock Borrow Program allows sellers to continue to fail to deliver because the Stock Borrow Program has effectively obviated the sellers' obligation to deliver and the buyers' right to buy-in through the market.

93. By borrowing shares through the Stock Borrow Program to cover fails to deliver, the Defendants have created tens of millions of unregistered illegal free trading shares of the issuer, artificially (1) increasing the supply of an issuer's shares in the marketplace; (2) driving down the price of the stock of the issuer; (3) devaluing the shareholders' holdings in an issuer's stock; and (4) causing multiple owners who purchase shares in separate transactions to own the same shares.

94. For example, assume that on April 1, Issuer has 100,000 issued and outstanding shares. On April 1, Seller S sells 1,000 shares of Issuer's stock to Buyer B. Seller S fails to deliver the 1,000 shares for settlement by April 4, which is Settlement Day. The NSCC then borrows 1,000 shares from Lender L through the Stock Borrow Program and delivers the 1,000 shares to Buyer B's Depository Trust account on April 4. Buyer B's Depository Trust account now reflects that Buyer B owns 1,000 shares. At the same time, since Lender L's loan of 1000 shares to the NSCC is not reported or visible to the marketplace, Lender L's NSCC account still reports that it owns the 1,000 shares that it lent to the NSCC. As a result, the marketplace now indicates that Issuer has 101,000 issued and outstanding shares, when in fact Issuer has NOT issued or authorized the additional 1,000

shares, These shares were artificially created by the NSCC when it borrowed 1,000 shares through the Stock Borrow Program and delivered them to Buyer B. Furthermore, two people now own the same 1,000 shares – Lender L and Buyer B.

95. Since the 1,000 shares received by Buyer B in the paragraph 58 illustration is now held in Buyer B's Depository Trust account, Buyer B can now lend the 1,000 shares to the NSCC through the Stock Borrow Program, thus, repealing the process and resulting in multiple shareholders owning the same shares. For example, assume that in a subsequent transaction on April 5, Seller S sells 750 shares of Issuer's stock to Buyer C. Seller S fails to deliver the 750 shares on April 8, Settlement Day. Therefore, the NSCC borrows 750 shares from Buyer B through the Stock Borrow Program and delivers the shares to Buyer C's Depository Trust account on April 8, which account now reflects that Buyer C owns 750 shares. In addition, since Buyer B's loan of 750 shares to the NSCC is not reported or visible to the marketplace, Buyer B's NSCC account still indicates that Buyer B owns the 750 shares which the NSCC borrowed for delivery to Buyer C. In sum, the marketplace now indicates that Issuer has 101,750 issued and outstanding shares, when in fact Issuer has NOT issued or authorized the additional 1,750 shares. These shares were artificially created by the NSCC when it borrowed 1,000 shares through the Stock Borrow Program for delivery to Buyer B and then borrowed 750 shares from Buyer B for delivery to Buyer C. Furthermore and most remarkably,

three people now own the same 750 shares – Lender L, Buyer B and Buyer C.

96. This process of recycling borrowed shares amounts to stock-kiting in that the same borrowed shares can continuously be transferred from a buyer and loaned to the NSCC for delivery to the next buyer who then loans the same shares to the NSCC and so forth. Thus, the same shares can be recycled repeatedly through the Stock Borrow Program to satisfy multiple delivery requirements.

97. The Stock Borrow Program allows the borrowed shares to be recycled repeatedly, resulting in the number of borrowed shares exceeding the number of shares issued and authorized by the issuer. In addition, upon information and belief, the number of borrowed shares exceeds the total number of issuer's shares actually on deposit at the Depository Trust.[5] Thus, upon information and belief, the Depository Trust owns and holds a significantly fewer number of lendable shares than the NSCC has borrowed through the Stock Borrow Program.

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5. As set forth in the letter from Ralph A. Lambaise, President, North American Securities Administrators Association, Inc., to Jonathan Katz, Secretary, Securities and Exchange Commission (January 5, 2004), the Securities and Exchange "Commission should explicitly prohibit the [Depository Trust] from lending more shares of a security than it actually holds."

98. This recycling of borrowed shares through the Stock Borrow Program could potentially result in a "run-on-the-bank" situation. If every shareholder (including shareholders who received borrowed shares) were to demand delivery of stock certificates by the Depository Trust, the custodian of the physical shares, there would be insufficient shares available for delivery because the Stock Borrow Program has artificially generated more shares than are physically held by the Depository Trust.

99. There is little incentive for the Defendants to force sellers to cure fail to deliver positions once the loan has been made because the Stock Borrow Program has become such a reliable source of income for the Defendants. For the year ended December 31, 2003, the Depository Trust reported revenues from services of $425,416,000 and the NSCC reported revenues from services of $293,133,000. In addition, open fail to deliver positions present a potential risk of loss to the Defendants because the NSCC covers these positions by borrowing shares through the Stock Borrow Program. At the close of business on December 31, 2003, the value of securities borrowed through the Stock Borrow Program was stated to be approximately $721,750,000. As a result, the NSCC, as borrower, has subjected itself to the possibility of significant financial losses if the seller is ultimately unable to honor its delivery obligations to the NSCC.

100. Through the Stock Borrow Program, the Defendants have permitted sellers to maintain fail to deliver positions of millions of shares for periods of a

year and even longer. This course of conduct by the Defendants has had the effect of creating tens of millions of additional unregistered illegal free trading shares of the issuer, artificially increasing the supply of shares in the marketplace and driving down and manipulating the price of the stock of numerous issuers, including Plaintiff Nanopierce.

AS AND FOR A FIRST CLAIM FOR RELIEF FOR VIOLATION OF NEVADA REVISED STATUTES 90.570 AND 90.660 MISREPRESENTATIONS AS TO THE NATURE OF THE STOCK BORROW PROGRAM

101. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 100 of the Complaint as if fully set forth herein.

102. Defendants have each misrepresented to the Plaintiffs that the NSCC is borrowing shares from lending Members of the Stock Borrow Program to cover fail to deliver positions in the clearing and settlement process, when, in fact, the transfer of shares from lending Members to the NSCC to cover such fail to deliver positions is actually a "sale" of securities. This transaction is actually a sale because the NSCC delivers the borrowed shares to the buyer who acquires all right, title and interest in the shares, including the right to vote, receive dividends and resell the shares, without further encumbrance or any reservation of rights.[6]

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6. As noted in NASD Proposed Amendments Relating to Short Sale Delivery Requirements (SR-NASD-2004-044), "significant failures to deliver can impact certain rights of buyers, such as the right to vote shares or the treatment of dividends".

103. The misrepresentations and omissions by the Defendants alleged above were false and misleading when made.

104. The misrepresentations and omissions of the Defendants as alleged above were material.

105. In making the misrepresentations and omissions, the Defendants acted with scienter. The Defendants have a major financial motivation to make the misrepresentations and omissions alleged herein because they have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public since questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

106. The misrepresentations and omissions by the Defendants were made in their Annual Statements, on their websites and various press releases issued to the investing public, which include the Plaintiffs.

107. In reliance upon these misrepresentations and omissions by Defendants, Plaintiffs traded Nanopierce shares, which trades were cleared and settled by and through the Defendants without knowledge of Defendants' violation of Nevada securities laws.

108. Alternatively, Plaintiffs relied on the Defendants' material and public misrepresentations and omissions and traded Nanopierce shares in the stock market

without knowledge of Defendants' fraud-on-the-market through the clearing and settlement services they provided.

109. DTCC, through its subsidiary, the NSCC and the Depository Trust, offers to sell and actually sells securities by means of communications which contain material misrepresentations and omissions, its violation of Nevada Revised Statutes 90.570 and NRS 90.660.

110. During the relevant period, the Defendants carried out a plan, scheme and course of conduct which was intended to, and throughout the period, did (i) deceive Plaintiffs; and (ii) cause Plaintiffs to purchase and/or sell Nanopierce shares at artificially depressed prices. In furtherance of this unlawful scheme, plan and course of conduct, Defendants each took the actions set forth herein which are in violation of Nevada Revised Statutes 90.570 and NRS 90.660.

111. The misrepresentations and omissions by the Defendants detailed above have damaged and injured Plaintiffs, which relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

112. As a result of the Defendants' violation of Nevada Revised Statutes 90.570 and NRS 90.660 and the wrongs herein alleged, Plaintiffs have suffered substantial damages in an amount to be proven at trial.

Appendix

AS AND FOR A SECOND CLAIM FOR RELIEF FOR VIOLATION OF NEVADA REVISED STATUTES 90.570 AND 90.660 MISREPRESENTATIONS REGARDING THE CLEARING AND SETTLEMENT OF TRADES

113. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 112 of the Complaint as if fully set forth herein.

114. The Defendants have each represented to Plaintiffs that they efficiently clear and settle trades. In fact, the DTCC, the NSCC and the Depository Trust are not clearing and settling trades that result in open fail to deliver positions because these trades are processed through the Stock Borrow Program and therefore remain unsettled for extended periods of time.

115. In connection with its services to the marketplace, the DTCC, itself and by and through the NSCC and the Depository Trust, made the following representations to Plaintiffs on its Annual Statements, its websites and various press releases:

(i) that through the CNS System, it maintains an orderly flow of security and money balances;

(ii) that through the Stock Borrow Program, Members lend NSCC stock from their accounts at the Depository Trust to cover temporary shortfalls in the CNS System; and

(iii) that securities loaned to the NSCC through the Stock Borrow Program enable the NSCC to satisfy CNS delivery obligations not filled through normal deliveries.

116. Notwithstanding these representations, upon information and belief, the Defendants are each aware that sellers routinely fail to deliver securities and that unfulfilled obligations to deliver securities can have negative effects on the market when fails to deliver persist for an extended period of time.

117. Further, the Defendants are each aware that Open fail to deliver positions covered by shares borrowed through the Stock Borrow Program actually increase the supply of shares in the marketplace by the number of shares borrowed, resulting in the artificial inflation of the issued and outstanding shares of issuers.

118. By utilizing the Stock Borrow Program to cover open fail to deliver positions in Nanopierce stock and consequently creating artificial Nanopierce shares, the Defendants have misrepresented to Plaintiffs that these artificial shares are issued and outstanding shares of Nanopierce, when in fact these shares have not been issued or authorized by Nanopierce. This misrepresentation by the Defendants adversely affected the sale of Nanopierce stock and was relied upon by Plaintiffs when deciding to purchase and/or sell Nanopierce shares.

119. The representations and omissions by the Defendants alleged above were false and misleading when made.

120. In making the misrepresentations and omissions, the Defendants acted with scienter. The Defendants have a major financial motivation to make the misrepresentations and omissions alleged herein because they have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public since questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

121. Defendants' misrepresentations and omissions, as alleged above were material.

122. In reliance upon these misrepresentations and omissions by Defendants, Plaintiffs traded Nanopierce shares, which trades were cleared and settled by and through the Defendants without knowledge of Defendants' violation of Nevada securities laws.

123. Alternatively, Plaintiffs relied on Defendants' material and public misrepresentations and omissions and traded Nanopierce shares in the stock market without knowledge of Defendants' fraud-on-the-market through statements they made about the clearing and settlement services they provided.

124. The Plaintiffs have suffered substantial damages from the Defendants' misrepresentation that they use the Stock Borrow Program to efficiently clear and settle trades, when in fact they are not using the Stock Borrow Program to clear and settle trades efficiently but rather

to mask inefficiencies in their clearance and settlement process by covering open fail to deliver positions with borrowed shares for millions of shares and extended periods of time. As a result, the Defendants have created additional unregistered and unauthorized Nanopierce shares and artificially increased the supply of Nanopierce shares in the marketplace and decreased the stock's value.

125. The misrepresentations and omissions by the Defendants detailed above are in violation of Nevada Revised Statutes 90.570 and NRS 90.660 and have damaged and injured Plaintiffs, which relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

126. As a result of the Defendants' violation of Nevada Revised Statutes 90.570 and NRS 90.660 and the wrongs herein alleged, Plaintiffs have suffered substantial damages in an amount to be proven at trial.

AS AND FOR A THIRD CLAIM FOR RELIEF FOR VIOLATION OF NEVADA REVISED STATUTES 90.570 AND 90.660 MISREPRESENTATIONS AS TO THE NUMBER OF SHARES HELD IN LENDING MEMBERS' NSCC AND DEPOSITORY TRUST ACCOUNTS

127. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 126 of the Complaint as if fully set forth herein.

128. The Defendants have misrepresented to Plaintiffs the number of Nanopierce shares actually held by the lending Members at the Depository Trust by providing misleading information in the lending Members' Depository Trust and NSCC account statements.

129. When shares are borrowed by the NSCC from a lending Member, the lending Member's Depository Trust account reflects a debit of the number and value of the shares borrowed and a balance which is minus the borrowed shares. The borrowed shares are credited to a separate account that reflects all the shares loaned by the lending Member. However, because the Depository Trust records the borrowing by balancing the aforementioned two accounts, the lending Member's total Depository Trust account is not reduced to exclude the number and value of the loaned shares. Therefore, when shares are borrowed, the lending Member's Depository Trust account misleadingly reflects an amount and value of shares that are not actually held by the lending Member at the Depository Trust.

130. Further, the NSCC records the borrowing of the shares by balancing the lending Member's CNS sub-accounts,[7] so that the net change in holdings of the

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7. The NSCC records the borrowing of the shares by creating a miscellaneous activity entry in the lending Member's CNS sub-accounts. The number of shares borrowed is journaled in the lending Member's CNS sub-account as a short position to show the delivery obligation of the lending Member to the NSCC for the number and value of the borrowed shares. This short position

(Cont'd)

lending Member is not reduced to exclude the number and value of the loaned shares. Therefore, when shares are borrowed, the lending Member's NSCC account statement misleadingly reflects an amount and value of shares that are not actually held by the lending Member at the Depository Trust.

131. But for Defendants' inaccurate and misleading accounting of the borrowed shares, the number of shares borrowed would not exceed the number of lendable shares on deposit with the Depository Trust.

132. The representations and omissions by the Defendants alleged above were false and misleading when made.

133. In making the misrepresentations and omissions, the Defendants acted with scienter. The Defendants have a major financial motivation to make the misrepresentations and omissions alleged herein because they have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public since questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust

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(Cont'd)

is automatically covered by taking the shares on deposit in the lending Member's Depository Trust account. A separate journal entry is made in another sub-account of the lending Member as a long position to show the number and value of the shares due to be returned by the NSCC to the lending Member. The long position is adjusted daily to reflect the market value of the borrowed shares.

and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

134. The misrepresentations and omissions of the Defendants, as alleged above, were material.

135. In reliance upon these misrepresentations and omissions by Defendants, Plaintiffs traded Nanopierce shares, which trades were cleared and settled by and through the Defendants and without knowledge of Defendants' violation of Nevada securities laws.

136. Alternatively, Plaintiffs relied on Defendants' material and public misrepresentations and omissions and traded Nanopierce shares in the stock market without knowledge of Defendants' fraud-on-the-market through the clearing and settlement services they provided.

137. The misrepresentations and omissions by the Defendants detailed above are in violation of Nevada Revised Statutes 90.570 and NRS 90.660 and have damaged and injured Plaintiffs, which relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

138. As a result of the Defendants' violation of Nevada Revised Statutes 90.570 and NRS 90.660 and the wrongs herein alleged, Plaintiffs have suffered substantial damages in an amount to be proven at trial.

AS AND FOR A FOURTH CLAIM FOR RELIEF FOR VIOLATION OF NEVADA REVISED STATUTES 90.570 AND 90.660 MISREPRESENTATIONS AS TO THE OPERATION OF THE STOCK BORROW PROGRAM

139. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 138 of the Complaint as if fully set forth herein.

140. The Defendants have represented to Plaintiffs that open fail to deliver positions will be cured by buying in the open positions with shares purchased from the marketplace, when in fact, these open positions are actually cured with shares borrowed from lending Members through the Stock Borrow Program.

141. As set forth in the Rules and Procedures of the National Securities Clearing Corporation (effective December 26, 2003), when a seller fails to deliver, the buyer notifies the NSCC that it intends to buy-in the seller's fail to deliver position. Instead of executing the buy-in by going into the market, the NSCC executes the buy-in by borrowing shares from lending Members of the Stock Borrow Program to satisfy the buyer's buy-in request and to cover the seller's fail to deliver position.

142. The representations and omissions by the Defendants alleged above were false and misleading when made.

143. In making the misrepresentations and omissions, the Defendants acted with scienter. The Defendants have

a major financial motivation to make the misrepresentations and omissions alleged herein because they have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public since questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

144. The misrepresentations and omissions of the Defendants, as alleged above, were material.

145. In reliance upon these misrepresentations and omissions by Defendants, Plaintiffs traded Nanopierce shares, which trades were cleared and settled through Defendants without knowledge of Defendants' violation of Nevada securities laws.

146. Alternatively, Plaintiffs relied on Defendants' material and public misrepresentations and omissions and traded Nanopierce shares in the stock market without knowledge of Defendants' fraud-on-the-market through the clearing and settlement services they provided.

147. The misrepresentations and omissions by the Defendants detailed above are in violation of Nevada Revised Statutes 90.570 and NRS 90.660 and have damaged and injured Plaintiffs, which relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

148. As a result of the Defendants' violation of Nevada Revised Statutes 90.570 and NRS 90.660 and the wrongs herein alleged, Plaintiffs have suffered substantial damages in an amount to be proven at trial.

AS AND FOR A FIFTH CLAIM FOR RELIEF FOR VIOLATION OF NEVADA REVISED STATUTES 90.580 AND 90.660 MARKET MANIPULATION

149. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 148 of the Complaint as if fully set forth herein.

150. Prior to the establishment of the Stock Borrow Program, the Defendants executed buy-ins by purchasing shares from the open market to cover open fail to deliver positions. These transactions involved a change in beneficial ownership of the affected shares and constituted a purchase and sale of securities which was reported and visible to the marketplace.

151. Since the institution of the Stock Borrow Program and as set forth in Addendum C-1, Rules and Procedures of the National Securities Clearing Corporation (effective December 26, 2003), instead of executing buy-ins by purchasing shares from the open market, the NSCC now executes buy-ins by borrowing shares through the Stock Borrow Program. When a buy-in is executed using shares borrowed through the Stock Borrow Program, the transaction is not reported or visible to the marketplace. This is because the transaction characterized by the NSCC as a loan under

the Stock Borrow Program does not involve a change in beneficial ownership, since borrowed shares are not deducted from a lending Member's total Depository Trust and NSCC account holdings.

152. The purpose of executing buy-ins by borrowing shares through the Stock Borrow Program instead of purchasing shares from the open market is to create a false and misleading appearance with respect to the market for Nanopierce stock.

153. By lending shares to sellers who have failed to deliver, the Defendants have manipulated the market by effecting a transaction in Nanopierce securities which involves no change in the beneficial ownership of the security for the purpose of creating a false or misleading appearance with respect to the market for Nanopierce stock.

154. The Defendants' execution of buy-ins with shares borrowed through the Stock Borrow Program is in violation of Nevada Revised Statutes 90.580 and NRS 90.660 and has damaged and injured the Plaintiffs.

155. As a result of the Defendants' violation of Nevada Revised Statutes 90.580 and NRS 90.660 and the wrongs herein alleged, Plaintiffs have suffered substantial damages in an amount to be proven at trial.

Appendix

AS AND FOR A SIXTH CLAIM FOR RELIEF FOR VIOLATION OF SECTION 598A.060 OF THE NEVADA UNFAIR TRADE PRACTICES ACT

156. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 155 of the Complaint as if fully set forth herein.

157. DTCC, through its subsidiaries, the NSCC and the Depository Trust, provides clearance and settlement services for its members.

158. The Stock Borrow Program purportedly improves the efficiency of the clearance and settlement function by addressing temporary fail to deliver situations. Under the Stock Borrow Program, if a seller fails to deliver shares on Settlement Day, the NSCC borrows the shares from willing lenders and gives the shares to the buyer in settlement of the trade. Membership in both the NSCC and Depository Trust is required in order to be a lender in the Stock Borrow Program.

159. The clearance and settlement services provided by the Defendants are completely separate and distinct from the functions of the Stock Borrow Program, and there is a separate market and demand for each of them.

160. The Defendants have illegally tied the Stock Borrow Program to the separate and distinct functions of clearing and settling stock trades by requiring that open fail to deliver positions be covered with shares borrowed through the Stock Borrow Program, either

directly through the NSCC's daily allocation cycle or indirectly through a buy-in executed with shares borrowed through the Stock Borrow Program.

161. The purpose and effect of this tying arrangement is to prevent buyers from entering the stock market to purchase shares to buy in open fail to deliver positions at competitive market prices, and instead requiring buyers to execute buy-ins through the Stock Borrow Program.

162. The conduct of the Defendants is anticompetitive since they have prevented buyers from entering the stock market to purchase shares to cover open fail to deliver positions, thereby unreasonably restraining competition in the market and violating the Nevada Unfair Trade Practices Act.

163. The tying arrangement is anticompetitive because it diverts to the Defendants the buyers' demand for shares to cover open fail to deliver positions by requiring buy-ins for open fail to deliver positions to be filled with shares borrowed through the Stock Borrow Program instead of allowing the demand to be filled by all market participants through buying in from the stock market.

164. The value of Nanopierce shares on the open market has been reduced by the Defendants' anticompetitive behavior because the supply of shares from buy-ins executed through the Stock Borrow Program is limited to lending Members rather than the open market of securities sellers as a whole. A buy-in executed by

entering the stock market includes all market participants and is based on the natural supply and demand for the borrowed security.

165. If the clearance and settlement functions of the Defendants were not tied to the Stock Borrow Program, buyers would be able to buy-in open fail to deliver positions by going into the stock market instead of having to execute their buy-in request through the Stock Borrow Program.

166. In addition, the transaction which underlies the Stock Borrow Program is actually a "sale" of securities by a member to the NSCC. This transaction is a sale because the NSCC delivers the borrowed shares to the buyer who acquires all right, title and interest in the shares, including the right to vote, receive dividends and resell the shares, without further encumbrance or any reservation or rights.[8] The Defendants have intentionally mischaracterized this transaction as a "loan" in order to disguise the anticompetitive nature of the transaction.

167. As a result of the Defendants' anticompetitive conduct in tying the Stock Borrow Program to the separate and distinct functions of clearing and settling stock trades, upon information and belief, buyers of Nanopierce shares in trades which resulted in open fail

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8. As noted in NASD Proposed Amendments Relating to Short Sale Delivery Requirements (SR-NASD-2004-044), "significant failures to deliver can impact certain rights of buyers, such as the right to vote shares or the treatment of dividends".

to deliver positions were prevented from entering the stock market to buy-in shares to cover these positions. Instead, these fail to deliver positions were required to be covered by shares borrowed through the Stock Borrow Program.

168. By requiring that buyers buy-in open fail to deliver positions with shares borrowed through the Stock Borrow Program and accepting delivery of t borrowed shares, the Defendants have artificially created unregistered, free trading Nanopierce shares and have increased the supply of Nanopierce shares in the marketplace without authority.

169. The artificially increased supply of Nanopierce shares in the marketplace created by the Defendants' anticompetitive conduct in tying the Stock Borrow Program to the separate and distinct functions of clearing and settling stock trades has significantly decreased the value of Nanopierce stock and Plaintiffs' holdings in Nanopierce stock.

170. The foregoing acts and practices, and the continuing course of the Defendants' anticompetitive conduct, have harmed the Plaintiffs.

171. The Defendants' conduct is anticompetitive. There are no procompetitive effects of this tying arrangement that might outweigh the harm to competition in the stock market.

172. As a direct result of the Defendants' illegal conduct, competition in the stock market has been restrained and suppressed.

173. Defendants' anticompetitive and exclusionary conduct has directly and proximately caused injury to Plaintiff Nanopierce's businesses and property and Plaintiffs Seitz's, Plaintiff Knight-McConnell's, Plaintiff Stock's, Plaintiff O'Sullivan's and Plaintiff Kolada's property as set forth above. Plaintiffs' injuries are the type the Nevada Unfair Trade Practices Act is intended to prevent and thus constitute unfair trade practice injuries.

174. As a result of the Defendants' violation of the Nevada Unfair Trade Practices Act and the wrongs herein alleged, Plaintiffs have suffered substantial damages in an amount to be proven at trial.

As and For a Seventh Claim for Relief for Negligent Misrepresentations as to the Nature of the Stock Bonus Program

175. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 174 of the Complaint as if fully set forth herein.

176. Defendants have misrepresented to Plaintiffs that the Stock Borrow Program is a "loan" of shares from participating members of the Stock Borrow Program to cover fail to deliver positions in the clearing and settlement process.

177. Defendants have failed to exercise reasonable care or competence in communicating to Plaintiffs that the NSCC is borrowing shares from lending Members

through the Stock Borrow Program to cover fail to deliver positions in the clearing and settlement process, when, in fact, the transfer of shares from lending Members to the NSCC to cover such fail to deliver positions is actually a "sale" of securities. This transaction is a sale because the NSCC delivers the borrowed shares to the buyer who acquires all right, title and interest in the shares, including the right to vote, receive dividends and resell the shares, without further encumbrance or any reservation of rights.[9]

178. The representations and omissions by the Defendants alleged above were false and misleading when made.

179. The misrepresentations and omissions by Defendants to Plaintiffs were made in their Annual Statements, on their websites and in various press releases.

180. The Defendants have a major financial motivation to make the misrepresentations and omissions. The Defendants have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public because questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

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9. As noted in NASD Proposed Amendments Relating to Short Sale Delivery Requirements (SR-NASD-2004-044), "significant failures to deliver can impact certain rights of buyers, such as the right to vote shares or the treatment of dividends".

181. The misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which justifiably relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

182. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

AS AND FOR AN EIGHTH CLAIM FOR RELIEF FOR NEGLIGENT MISREPRESENTATIONS REGARDING THE CLEARING AND SETTLEMENT OF TRADES

183. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 182 of the Complaint as if fully set forth herein.

184. The Defendants have failed to exercise reasonable care or competence in communicating to Plaintiffs that they efficiently clear and settle trades. In fact, the Defendants are not clearing and settling those trades which result in open fail to deliver positions, because these trades are processed through the Stock Borrow Program and remain unsettled for extended periods of time.

185. In connection with its services to the marketplace, the DTCC, itself and by and through the NSCC and the Depository Trust, have further communicated to Plaintiffs the following representations on its Annual Statements, its websites and various press releases:

(i) that through the CNS System, it maintains an orderly flow of security and money balances;

(ii) that through the Stock Borrow Program, Members lend NSCC stock from their accounts at the Depository Trust to cover temporary shortfalls in the CNS System; and

(iii) that securities loaned to the NSCC through the Stock Borrow Program, enable the NSCC to satisfy CNS delivery obligations not filled through normal deliveries.

186. Notwithstanding these representations, upon information and belief, the Defendants are aware that sellers routinely fail to deliver securities on Settlement Day and that unfulfilled obligations to deliver securities can have negative effects on the market when fails to deliver persist for an extended period of time.

187. Further, the Defendants are aware that open fail to deliver positions covered by shares borrowed through the Stock Borrow Program actually increase the supply of shares in the marketplace by the number of shares borrowed, resulting in the artificial inflation of the issued and outstanding shares of the issuer.

188. By utilizing the Stock Borrow Program to cover open fail to deliver positions in Nanopierce stock and consequently creating artificial Nanopierce shares, the Defendants have negligently misrepresented to Plaintiffs that these artificial shares are issued and outstanding shares of Nanopierce, when in fact these

shares have not been issued or authorized by Nanopierce. This misrepresentation by the Defendants adversely affected the sale of Nanopierce stock and was justifiably relied upon by Plaintiffs when deciding to purchase and/or sell Nanopierce shares.

189. The representations and omissions by the Defendants alleged above were false and misleading when made.

190. Defendants have a major financial motivation to make the misrepresentations and omissions alleged above. Defendants have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public because questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

191. The Plaintiffs have suffered substantial damages from the Defendants' misrepresentation that they use the Stock Borrow Program to efficiently clear and settle trades, when in fact they are not using the Stock Borrow Program to clear and settle trades efficiently but rather to mask inefficiencies in their clearance and settlement process by covering open fail to deliver positions with borrowed shares involving millions of shares for extended periods of time. As a result, the Defendants have created additional unregistered and unauthorized Nanopierce shares and have artificially increased the supply of Nanopierce shares in the marketplace and decreased the value of said stock.

192. The negligent misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which justifiably relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

193. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

AS AND FOR A NINTH CLAIM FOR RELIEF FOR NEGLIGENT MISREPRESENTATIONS AS TO THE NUMBER OF SHARES HELD IN LENDING MEMBERS' NSCC AND DEPOSITORY TRUST ACCOUNTS

194. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 193 of the Complaint as if fully set forth herein.

195. Defendants have failed to exercise reasonable care or competence in communicating to Plaintiffs the number of Nanopierce shares actually held by the lending Members at the Depository Trust by providing misleading information in the lending Members' Depository Trust and NSCC account statements.

196. When shares are borrowed by the NSCC from a lending Member, the lending Member's Depository Trust account reflects a debit of the number and value of the shares borrowed and a balance which is minus the borrowed shares. The borrowed shares are credited to a separate account that reflects all the shares loaned by

the lending Member. However, because the Depository Trust records the borrowing by balancing the aforementioned two accounts, the lending Member's total Depository Trust account is not reduced to exclude the number and value of the loaned shares. Therefore, when shares are borrowed, the lending Member's Depository Trust account misleadingly reflects an amount and value of shares that are not actually held by the lending Member at the Depository Trust.

197. Further, the NSCC records the borrowing of the shares by balancing the lending Member's CNS sub-accounts,[10] so that the net change in holdings of the lending Member is not reduced to exclude the number and value of the loaned shares. Therefore, when shares are borrowed, the lending Member's NSCC account statement misleadingly reflects an amount and value of shares that are not actually held by the lending Member at the Depository Trust.

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10. The NSCC records the borrowing of the shares by creating a miscellaneous activity entry in the lending Member's CNS sub-accounts. The number of shares borrowed is journaled in the lending Member's CNS sub-account as a short position to show the delivery obligation of the lending Member to the NSCC for the number and value of the borrowed shares. This short position is automatically covered by taking the shares on deposit in the lending Member's Depository Trust acount. A separate journal entry is made in another sub-account of the lending Member as a long position to show the number and value of the shares due to be returned by the NSCC to the lending Member. The long position is adjusted daily to reflect the market value of the borrowed shares.

198. But for Defendants' inaccurate and misleading accounting of the borrowed shares, the number of shares borrowed would not exceed the number of lendable shares on deposit with the Depository Trust.

199. The representations and omissions by the Defendants alleged above were false and misleading when made.

200. Defendants have a major financial motivation to make the misrepresentations and omissions alleged above.

201. Defendants have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public because questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

202. The negligent misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which justifiably relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

203. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

Appendix

AS AND FOR A TENTH CLAIM FOR RELIEF FOR NEGLIGENT MISREPRESENTATIONS AS TO THE OPERATION OF THE STOCK BORROW PROGRAM

204. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 203 of the Complaint as if fully set forth herein.

205. Defendants have failed to exercise reasonable care or competence in communicating to Plaintiffs that open fail to deliver positions will be cured by buying in the open positions with shares purchased from the marketplace, when in fact, these open positions are actually cured with shares borrowed from lending Members through the Stock Borrow Program.

206. As set forth in the Rules and Procedures of the National Securities Clearing Corporation (effective December 26, 2003), when a seller fails to deliver, the buyer notifies the NSCC that it intends to buy-in the seller's fail to deliver position. Instead of executing the buy-in by going into the market, the NSCC executes the buy-in by borrowing shares from lending Members of the Stock Borrow Program to satisfy the buyer's buy-in request and to cover the seller's fail to deliver position.

207. The representations and omissions by the Defendants alleged above were false and misleading when made.

208. Defendants have a major financial motive to allow the misrepresentations and omissions to be made.

209. Defendants have a major economic incentive to keep knowledge of the fail to deliver problem out of the awareness of the investing public because questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

210. The negligent misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which justifiably relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

211. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

As and For an Eleventh Claim for Relief for Intentional Misrepresentations as to the Nature of the Stock Borrow Program

212. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 211 of the Complaint as if fully set forth herein.

213. Defendants have willfully and/or recklessly represented to Plaintiffs that the NSCC is borrowing shares from lending Members of the Stock Borrow Program to cover fail to deliver positions in the clearing

and settlement process, when, in fact, the transfer of shares from lending Members to the NSCC to cover such fail to deliver positions is actually a "sale" of securities. This transaction is a sale because the NSCC delivers the borrowed shares to the buyer who acquires all right, title and interest in the shares, including the right to vote, receive dividends and resell the shares, without further encumbrance or any reservation of rights.[11]

214. The representations and omissions by Defendants alleged above were false and misleading when made.

215. The misrepresentations and omissions by Defendants were willfully and/or recklessly made in their Annual Statements, on their websites and in various press releases issued to the investing public, which include the Plaintiffs.

216. Defendants have a major financial motivation to make the misrepresentations and omissions. Defendants have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public because questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

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11. As noted in NASD Proposed Amendments Relating to Short Sale Delivery Requirements (SR-NASD-2004-044), "significant failures to deliver can impact certain rights of buyers, such as the right to vote shares or the treatment of dividends".

217. The intentional misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which justifiably relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

218. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

As and For a Twelfth Claim for Relief for Intentional Misrepresentations Regarding the Clearing and Settlement of Trades

219. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 218 of the Complaint as if fully set forth herein.

220. Defendants have willfully and/or recklessly misrepresented to Plaintiffs that they efficiently clear and settle trades. In fact, the Defendants are not clearing and settling those trades which result in open fail to deliver positions because these trades are processed through the Stock Borrow Program and remain unsettled for extended periods of time.

221. In connection with its services to the marketplace, the Defendants have further willfully and/or recklessly represented to Plaintiffs the following representations on its Annual Statements, its websites and various press releases:

(i) that through the CNS System, it maintains an orderly flow of security and money balances;

(ii) that through the Stock Borrow Program, Members lend NSCC stock from their accounts at the Depository Trust to cover temporary shortfalls in the CNS System; and

(iii) that securities loaned to the NSCC through the Stock Borrow Program, enable the NSCC to satisfy CNS delivery obligations not filled through normal deliveries.

222. Notwithstanding these representations, upon information and belief, the Defendants are aware that sellers routinely fail to deliver securities on required Settlement Days and that unfulfilled obligations to deliver securities can have negative effects on the market when fails to deliver persist for an extended period of time.

223. Further, the Defendants are aware that open fail to deliver positions covered by shares borrowed through the Stock Borrow Program actually increase the supply of shares in the marketplace by the number of shares borrowed, resulting in the artificial inflation of the issued and outstanding shares of the issuer.

224. By utilizing the Stock Borrow Program to cover open fail to deliver positions in Nanopierce stock and consequently create artificial Nanopierce shares, the Defendants have misrepresented to the Plaintiffs that these artificial shares are issued and outstanding shares

of Nanopierce, when in fact these shares have not been issued or authorized by Nanopierce. This misrepresentation by the Defendants adversely affected the sale of Nanopierce stock and was justifiably relied upon by Plaintiffs when making decisions to purchase and/or sell Nanopierce shares.

225. The representations and omissions by Defendants alleged above were false and misleading when made.

226. Defendants have a major financial motivation to make the misrepresentations and omissions. Defendants have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public because questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

227. The Plaintiffs have suffered substantial damages from the Defendants' willful and/or reckless misrepresentation that they use the Stock Borrow Program to efficiently settle and clear trades, when in fact they are not using the Stock Borrow Program to clear and settle trades efficiently but rather to mask inefficiencies in their clearance and settlement process by covering open fail to deliver positions with borrowed shares for millions of shares and extended periods of time. As a result, the Defendants have created additional unregistered and unauthorized Nanopierce shares artificially increasing the supply of Nanopierce shares in the marketplace and decreasing the value of the stock.

228. The intentional misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which justifiably relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

229. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

As and For a Thirteenth Claim for Relief for Intentional Misrepresentations as to the Number of Shares Held in Lending Members' NSCC and Depository Trust Accounts

230. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 229 of the Complaint as if fully set forth herein.

231. Defendants have willfully and/or recklessly misrepresented to Plaintiffs the number of Nanopierce shares actually held by the lending Members at the Depository Trust by providing misleading information in the lending Members' Depository Trust and NSCC account statements.

232. When shares are borrowed by the NSCC from a lending member, the lending Member's Depository Trust account reflects a debit of the number and value of the shares borrowed and a balance which is minus the borrowed shares. The borrowed shares are credited to a separate account that reflects all the shares loaned by

the lending Member. However, because the Depository Trust records the borrowing by balancing the aforementioned two accounts, the lending Member's total Depository Trust account is not reduced to exclude the number and value of the loaned shares. Therefore, when shares are borrowed, the lending Member's Depository Trust account misleadingly reflects an amount and value of shares that are not actually held by the lending Member at the Depository Trust.

233. Further, the NSCC records the borrowing of the shares by balancing the lending Member's CNS sub-accounts,[12] so that the net change in holdings of the lending Member is not reduced to exclude the number and value of the loaned shares. Therefore, when shares are borrowed, the lending Member's NSCC account statement misleadingly reflects an amount and value of shares that are not actually held by the lending Member at the Depository Trust.

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12. The NSCC records the borrowing of the shares by creating a miscellaneous activity entry in the lending Member's CNS sub-accounts. The number of shares borrowed is journaled in the lending Member's CNS sub-account as a short position to show the delivery obligation of the lending Member to the NSCC for the number and value of the borrowed shares. This short position is automatically covered by taking the shares on deposit in the lending Member's Depository Trust account. A separate journal entry is made in another sub-account of the lending Member as a long position to show the number and value of the shares due to be returned by the NSCC to the lending Member. The long position is adjusted daily to reflect the market value of the borrowed shares.

234. But for Defendants' willful and/or reckless inaccurate and misleading accounting of the borrowed shares, the number of shares borrowed would not exceed the number of lendable shares on deposit with the Depository Trust.

235. The representations and omissions by Defendants alleged above were false and misleading when made.

236. Defendants have a major financial motivation to make the misrepresentations and omissions. Defendants have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public because questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

237. The intentional misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which justifiably relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

238. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

Appendix

As and For a Fourteenth Claim for Relief for Intentional Misrepresentations as to the Operation of the Stock Borrow Program

239. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 238 of the Complaint as if fully set forth herein.

240. Defendants have willfully and/or recklessly misrepresented to Plaintiffs that open fail to deliver positions will be cured through buy-ins, when in fact, these fail to deliver positions are actually cured by borrowing shares from lending Members through the Stock Borrow Program.

241. As set forth in the Rules and Procedures of the National Securities Clearing Corporation (effective December 26, 2003), when a seller fails to deliver, the buyer notifies the NSCC that it intends to buy-in the seller's fail to deliver position. Instead of executing the buy-in by going into the market, the NSCC executes the buy-in by borrowing shares from lending Members of the Stock Borrow Program to satisfy the buyer's buy-in request and to cover the seller's open fail to deliver position.

242. The representations and omissions by Defendants alleged above were false and misleading when made.

243. Defendants have a major financial motive to allow the misrepresentations and omissions to be made. Defendants have a major economic incentive to keep

knowledge of the fail to deliver problem out of the awareness of the investing public because questions or doubts as to the efficiency of the DTCC, NSCC, Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

244. The intentional misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which justifiably relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

245. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

As and For a Fifteenth Claim for Relief for Fraudulent Misrepresentations as to the Nature of the Stock Borrow Program

246. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 245 of the Complaint as if fully set forth herein.

247. Defendants have fraudulently represented to Plaintiffs that the NSCC is borrowing shares from lending Members of the Stock Borrow Program to cover fail to deliver positions in the clearing and settlement process, when, in fact, the transfer of shares from lending Members to the NSCC to cover such fail to deliver positions is actually a "sale" of securities. This transaction is a sale because the NSCC delivers the

borrowed shares to the buyer who acquires all right, title and interest in the shares, including the right to vote, receive dividends and resell the shares, without further encumbrance or any reservation of rights.[13]

248. The representations and omissions by Defendants alleged above were false and misleading when made.

249. The misrepresentations and omissions by Defendants were made in their Annual Statements, on their websites and in various press releases issued to the investing public, which include the Plaintiffs.

250. Defendants have a major financial motivation to make the misrepresentations and omissions. Defendants have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public because questions or doubts as to the efficiency of the DTCC, the NSCC, the Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

251. The fraudulent misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

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13. As noted in NASD Proposed Amendments Relating to Short Sale Delivery Requireents (SR-NASD-2004-044), "significant failures to deliver can impact certain rights of buyers, such as the right to vote shares or the treatment of dividends".

252. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

AS AND FOR A SIXTEENTH CLAIM FOR RELIEF FOR FRAUDULENT MISREPRESENTATIONS REGARDING THE CLEARING AND SETTLEMENT OF TRADES

253. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 252 of the Complaint as if fully set forth herein.

254. Defendants have fraudulently represented to Plaintiffs that they efficiently clear and settle trades. In fact, Defendants are not clearing and settling those trades which result in open "fail to deliver," positions because those trades are processed through the Stock Borrow Program and therefore remain unsettled for extended periods of time.

255. In connection with its services to the marketplace, the Defendants have further falsely represented to Plaintiffs the following representations on its Annual Statements, its websites and various press releases:

(i) that through the CNS System, it maintains an orderly flow of security and money balances;

(ii) that through the Stock Borrow Program, Members lend NSCC stock from their accounts at the Depository Trust to cover temporary shortfalls in the CNS System; and

(iii) that securities loaned to the NSCC through the Stock Borrow Program, enable the NSCC to satisfy CNS delivery obligations not filled through normal deliveries.

256. Notwithstanding these representations, upon information and belief, the Defendants are aware that sellers routinely fail to deliver securities on required Settlement Days and that unfulfilled obligations to deliver securities can have negative effects on the market when fails to deliver persist for an extended period of time.

257. Further, the Defendants are aware that open fail to deliver positions covered by shares borrowed through the Stock Borrow Program actually increase the supply of shares in the marketplace by the number of shares borrowed, resulting in the artificial inflation of the issued and outstanding shares of the issuer.

258. By utilizing the Stock Borrow Program to cover open fail to deliver positions in Nanopierce stock and consequently create artificial Nanopierce shares, the Defendants have misrepresented to the Plaintiffs that these artificial shares are issued and outstanding shares of Nanopierce, when in fact these shares have not been issued or authorized by Nanopierce. This misrepresentation by the Defendants adversely affected the sale of Nanopierce stock and was relied upon by Plaintiffs when making decisions to purchase and/or sell Nanopierce shares.

259. The representations and omissions by Defendants alleged above were false and misleading when made.

260. Defendants have a major financial motivation to make the misrepresentations and omissions. Defendants have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public because questions or doubts as to the efficiency of the DTCC, NSCC, Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

261. The Plaintiffs have suffered substantial damages as a result of the Defendants' misrepresentation that they use the Stock Borrow Program to efficiently settle and clear trades, when in fact they are not using the Stock Borrow Program to clear and settle trades efficiently but rather to mask inefficiencies in their clearance and settlement process by covering open fail to deliver positions with borrowed shares for millions of shares and extended periods of time. As a result, the Defendants have created additional unregistered and unauthorized Nanopierce shares and have artificially increased the supply of Nanopierce stock in the marketplace and decreased the value of the stock.

262. The fraudulent misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

263. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

As and For a Seventeenth Claim for Relief for Fraudulent Misrepresentations as to the Number of Shares Held in Lending Members' NSCC and Depository Trust Accounts

264. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 263 of the Complaint as if fully set forth herein.

265. Defendants have fraudulently represented to Plaintiffs the number of Nanopierce shares actually held by the lending Members at the Depository Trust by providing misleading information in the lending Members' Depository Trust and NSCC account statements.

266. When shares are borrowed by the NSCC from a lending Member, the lending Member's Depository Trust account reflects a debit of the number and value of the shares borrowed and a balance which is minus the borrowed shares. The borrowed shares are credited to a separate account that reflects all the shares loaned by the lending Member. However, because the Depository Trust records the borrowing by balancing the aforementioned two accounts, the lending Member's total Depository Trust account is not reduced to exclude the number and value of the loaned shares. Therefore, when shares are borrowed, the lending Member's

Depository Trust account misleadingly reflects an amount and value of shares that are not actually held by the lending Member at the Depository Trust.

267. Further, the NSCC records the borrowing of the shares by balancing the lending Member's CNS sub-accounts,[14] so that the net change in holdings of the lending Member is not reduced to exclude the number and value of the loaned shares. Therefore, when shares are borrowed, the lending Member's NSCC account statement misleadingly reflects an amount and value of shares that are not actually held by the lending Member at the Depository Trust.

268. But for Defendants' false and misleading accounting of the borrowed shares, the number of shares borrowed would not exceed the number of lendable shares on deposit with the Depository Trust.

269. The representations and omissions by Defendants alleged above were false and misleading when made.

---

14. The NSCC records the borrowing of the shares by creating a miscellaneous activity entry in the lending Member's CNS sub-accounts. The number of shares borrowed is journaled in the lending Member's CNS sub-account as a short position to show the delivery obligation of the lending Member to the NSCC for the number and value of the borrowed shares. This short position is automatically covered by taking the shares on deposit in the lending Member's Depository Trust account. A separate journal entry is made in another sub-account of the lending Member as a long position to show the number and value of the shares due to be returned by the NSCC to the lending Member. The long position is adjusted daily to reflect the market value of the borrowed shares.

270. Defendants have a major financial motivation to make the misrepresentations and omissions. Defendants have a significant economic incentive to keep knowledge of the fail to deliver problem away from the investing public because questions or doubts as to the efficiency of the DTCC, NSCC, Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

271. The fraudulent misrepresentations and omissions by the Defendants detailed above have damaged and injured Plaintiffs, which relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

272. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

As and For an Eighteenth Claim for Relief for Fraudulent Misrepresentations as to the Operation of the Stock Borrow Program

273. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 272 of the Complaint as if fully set forth herein.

274. Defendants have fraudulently represented to Plaintiffs that open fail to deliver positions will be cured by buying in the open positions with shares purchased from the marketplace, when in fact, these open positions are actually cured with shares borrowed from lending Members through the Stock Borrow Program.

275. As set forth in the Rules and Procedures of the National Securities Clearing Corporation (effective December 26, 2003), when a seller fails to deliver, the buyer notifies the NSCC that it intends to buy-in the seller's fail to deliver position. Instead of executing the buy-in by going into the market, the NSCC executes the buy-in by borrowing shares from lending Members of the Stock Borrow Program to satisfy the buyer's buy-in request and to cover the seller's open fail to deliver position.

276. The representations and omissions by Defendants alleged above were false and misleading when made.

277. Defendants have a major financial motive to allow the misrepresentations and omissions to be made. Defendants have a major economic incentive to keep knowledge of the fail to deliver problem out of the awareness of the investing public because questions or doubts as to the efficiency of the DTCC, NSCC, Depository Trust and their systems would jeopardize the $947 million fee-based revenues generated by the DTCC.

278. The fraudulent misrepresentations and omissions by Defendants detailed above have damaged and injured Plaintiffs, which relied on those misrepresentations and omissions in connection with the purchase and/or sale of Nanopierce shares.

279. Plaintiffs have suffered substantial damages as a result of the wrongs herein alleged in an amount to be proven at trial.

Appendix

AS AND FOR A NINETEENTH CLAIM FOR RELIEF FOR CONVERSION

280. Plaintiff Seitz, Plaintiff Knight-McConnell, Plaintiff Stock, Plaintiff O'Sullivan and Plaintiff Kolada repeat and reallege each and every allegation contained in paragraphs 1 through 279 of the Complaint as if fully set forth herein.

281. Upon information and belief, the Defendants, through the Stock Borrow Program, borrowed shares of Nanopierce stock from lending Members in order to cover open fail to deliver positions. The NSCC then delivered these Nanopierce shares to buyers. Upon delivery, the buyer acquired all right, title and interest in the Nanopierce shares, including the right to vote, receive dividends and resell the shares, without encumbrance or any reservation of rights.[15] This transaction was actually a sale of Nanopierce shares and not a loan. As a result, the Defendants exercised a wrongful and unauthorized dominion and control over the aforesaid borrowed Nanopierce shares, since the Defendants do not own the shares and have no right to transfer them.

282. Further, the Defendants have not obtained consent of the beneficial owners of the shares borrowed and transferred through the Stock Borrow Program.

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15. As noted in NASD Proposed Amendments Relating to Short Sale Delivery Requirements (SR-NASD-2004-044), "significant failures to deliver can impact certain rights of buyers, such as the right to vote shares or the treatment of dividends".

283. Upon information and belief, Plaintiff Seitz's, Plaintiff Knight-McConnell's, Plaintiff Stock's, Plaintiff O'Sullivan's and Plaintiff Kolada's shares were borrowed and transferred by the DTCC, the NSCC and the Depository Trust through the Stock Borrow Program without their consent. By borrowing shares without Plaintiff Seitz's, Plaintiff Knight-McConnell's, Plaintiff Stock's, Plaintiff O'Sullivan's and Plaintiff Kolada's consent, the Defendants have exerted a wrongful dominion and control over the borrowed shares which is inconsistent with the rights of Plaintiffs Seitz , Plaintiff Knight-McConnell, Plaintiff Stock, Plaintiff O'Sullivan and Plaintiff Kolada and therefore constitutes a conversion of the borrowed shares.

284. The Defendants, through the implementation of the Stock Borrow Program, allowed an unlimited number of shares to be borrowed for an unlimited period of time. Because of this, the Stock Borrow Program actually increased the supply of shares of Nanopierce stock in the marketplace by the number of shares borrowed.

285. As a result, the Defendants have created additional unregistered and unauthorized Nanopierce shares and artificially increased the supply of Nanopierce shares in the marketplace and decreased the value of the stock.

286. The Defendants' conversion of Plaintiff Seitz's, Plaintiff Knight-McConnell's, Plaintiff Stock's, Plaintiff O'Sullivan's and Plaintiff Kolada's shares through borrowing in the Stock Borrow Program decreased the value of Nanopierce stock and thus damaged the value

of Nanopierce shares held by Plaintiff Seitz, Plaintiff Knight-McConnell, Plaintiff Stock, Plaintiff O'Sullivan and Plaintiff Kolada.

287. As a result of the wrong alleged herein, Plaintiff Seitz, Plaintiff Knight-McConnell, Plaintiff Stock, Plaintiff O'Sullivan and Plaintiff Kolada have suffered damages in an amount representing the value of the stock prior to the conversion minus the value of the stock after the conversion.

As and For a Twentieth Claim for Relief for Intentional Interference with Contractual Relations Between Nanopierce and its Shareholders

288. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 287 of the Complaint as if fully set forth herein.

289. The operation of the Stock Borrow Program by the Defendants is an intentional interference with Nanopierce's contractual relationships with its shareholders, including but not limited to Plaintiff Seitz, Plaintiff Knight-McConnell, Plaintiff Stock, Plaintiff O'Sullivan and Plaintiff Kolada.

290. The Articles of Incorporation of Nanopierce constitute a contract between Nanopierce and its shareholders which sets forth the number of shares Nanopierce is authorized to issue.

291. The Defendants are aware of the existence and terms of this contract, since the Articles of Incorporation of Nanopierce are public records on file with the Nevada Secretary of State. Further, Nanopierce is a public company that is required to make public filings to the Securities and Exchange Commission and consequently information regarding Nanopierce is widely available.

292. The operation of the Stock Borrow Program by Defendants is an intentional interference with the contractual relationship between Nanopierce and its shareholders.

293. The operation of the Stock Borrow Program by the Defendants has interfered with and contravened the terms of Nanopierce's Articles of Incorporation because by covering open fail to deliver positions with shares borrowed through the Stock Borrow Program and delivering the borrowed shares to the Buy Side Members, the NSCC has artificially created unauthorized, unregistered, free trading Nanopierce shares. This constitutes a clear contravention of Nanopierce's Articles of Incorporation and contractual relationship with its shareholders, including but not limited to Plaintiff Seitz, Plaintiff Knight-McConnell, Plaintiff Stock, Plaintiff O'Sullivan and Plaintiff Kolada.

294. By covering open fail to deliver positions with shares borrowed through the Stock Borrow Program, the NSCC, as borrower, has subjected itself to the possibility of significant financial losses if the sellers are ultimately unable to honor their delivery obligations.

Therefore, the Defendants have motive to continue to operate the Stock Borrow Program in order to manipulate downward the price of Nanopierce's stock and reduce the market value of the open fail to deliver positions created by sellers.

295. The interference with Nanopierce's Articles of Incorporation by Defendants' creation of artificial additional Nanopierce shares through the Stock Borrow Program has damaged Nanopierce and its shareholders. The creation of unauthorized Nanopierce shares has caused an increase in the supply of such Nanopierce shares in the marketplace, which has significantly decreased the value of Nanopierce shares held by its shareholders, including but not limited to Plaintiff Seitz, Plaintiff Knight-McConnell, Plaintiff Stock, Plaintiff O'Sullivan and Plaintiff Kolada.

296. As a result, Nanopierce and its shareholders, including but not limited to Plaintiff Seitz, Plaintiff Knight-McConnell, Plaintiff Stock, Plaintiff O'Sullivan and Plaintiff Kolada have suffered substantial damages in an amount to be proven at trial.

As and For a Twenty-First Claim for Relief for Breach of Implied Covenant of Good Faith and Fair Dealing

297. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 296 of the Complaint as if fully set forth herein.

298. Nanopierce stock certificates constitute a contract between Nanopierce and the shareholder named on the stock certificate.

299. The Depository Trust is a shareholder of Nanopierce.

300. Upon information and belief, as of April 5, 2004, Depository Trust held, in trust, in its nominee name, Cede & Co., 53,503,305 shares of Nanopierce stock.

301. As a trustee and shareholder of Nanopierce shares, the Depository Trust is required to lawfully hold Nanopierce's shares.

302. Nanopierce relied on the Depository Trust, as shareholder and trustee of its shares, to act in good faith when holding its shares.

303. By permitting shares of Nanopierce to be diluted through the operation of the Stock Borrow Program, the Depository Trust has breached the implied covenant of good faith and fair dealing.

304. As a result, Nanopierce has suffered substantial damages in an amount to be proven at trial.

AS AND FOR A TWENTY-SECOND CLAIM FOR RELIEF FOR CONSPIRACY

305. Plaintiffs repeat and reallege each and every allegation contained in paragraphs 1 through 304 of the Complaint as if fully set forth herein.

306. The DTCC, the NSCC and the Depository Trust acted in concert to operate the Stock Borrow Program for the purpose of manipulating the price of Nanopierce stock.

307. By permitting shares of Nanopierce to be borrowed through the Stock Borrow Program, the DTCC, the NSCC and the Depository Trust have conspired to drive down the price of Nanopierce stock.

308. Upon information and belief, the price of Nanopierce stock fell because the operation of the Stock Borrow Program by the Defendants allowed the manipulation of Nanopierce stock by various sellers who failed to deliver Nanopierce shares.

309. The Defendants conspired to maintain significant open fail to deliver positions of millions of shares of Nanopierce stock for extended periods of time by implementing the Stock Borrow Program to cover these open and unsettled positions.

310. By covering open fail to deliver positions with shares borrowed through the Stock Borrow Program and delivering the borrowed shares to the buyers, the Defendants artificially created unregistered, free trading Nanopierce shares and increased the supply of Nanopierce shares in the marketplace without authority.

311. The artificially increased supply of Nanopierce shares in the marketplace created by the NSCC's and Depository Trust's borrowing of Nanopierce shares

through the Stock Borrow Program to cover open fail to deliver positions caused a dramatic devaluation of Nanopierce stock that would not have occurred absent the actions of Defendants as described herein.

276. As a result, Plaintiffs have suffered substantial damages in an amount to be proven at trial.

Prayer for Relief

WHEREFORE, Plaintiffs demand judgment in its favor and against the Defendants as follows:

a. Damages in an amount in excess of $10,000 in favor of each Plaintiff and against each Defendant;

b. Treble damages under the Nevada Unfair Trade Practices Act;

c. An accounting of all profits which inured to Defendants as a result of their scheme and disgorgement of those profits to Plaintiffs;

d. Attorneys' fees, expert witness fees, and costs, as allowed by law;

e. Pre-judgment and post-judgment interest at the maximum rate allowed by law;

f. Exemplary, special and punitive damages from all Defendants;

g. Costs incurred; and

h. Such other and further relief the Court deems just and proper.

Dated: May 11, 2004

Respectfully submitted,

By: s/ Dan C. Bowen

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IN THE

Supreme Court of the United States

NANOPIERCE TECHNOLOGIES, INC. (N/K/A VYTA CORP.), KATHY-KNIGHT MCCONNELL, HELEN KOLADA, MAUREEN O'SULLIVAN, JANE SEITZ, STEPHEN SEITZ, AND JAMES STOCK,

Petitioners,

v.

DEPOSITORY TRUST AND CLEARING CORPORATION, DEPOSITORY TRUST COMPANY, AND NATIONAL SECURITIES CLEARING CORPORATION,

Respondents.

On Petition for a Writ of Certiorari to the Supreme Court of Nevada

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April 15, 2008

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Respondent clearing corporations' own website has long represented that they operate the stock borrow program only "to cover temporary shortfalls" in the delivery of shares sold by parties to securities transactions.[1] That is a false representation. There is nothing "temporary" about respondents' practice of permitting fails-to-deliver for tens of millions of shares to persist for months and even years. Nor do temporary shortfalls explain respondents' misrepresentations and failures to disclose their related practice of permitting the same shares in the stock borrow program to be re-lent electronically over and over, so that multiple persons are deemed to "own" the same shares.

State-law prohibitions against false statements like these are fundamental to ensuring the protection of investors and companies and ensuring the protection of the securities markets. But the court below effectively cast aside Congress's long-standing mandate of dual regulation of the securities markets, as declared in the savings clauses in both the 1933 and 1934 Acts, which Congress left fully intact in its 1975 amendments to the federal securities laws.

Both of respondents' practices – which substantially benefit the Wall Street investment banks and similar entities that own and control the respondent clearing corporations – have resulted in an artificial increase of shares in the electronic marketplace far beyond the number of shares that public companies have validly issued. According to petitioners' complaint, which the Court must accept as true, respondents misrepresented and concealed those and other material facts. Respondents are liable for any resulting

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[1] NSCC, http://www.nscc.com/clearance/.

damages under state common-law prohibitions against misrepresentation that are as old as the nation and that further the policy of full disclosure underlying federal securities law.

To allow preemption of petitioners' quintessential common-law claims would upset classic preemption principles that this Court has often explained, but that numerous lower courts, including the court below, have misapplied. That confusion has led to both specific conflict and general confusion among the lower courts. Review by this Court is therefore warranted, and this case presents an excellent vehicle for the Court to clarify proper conflict-preemption analysis for state securities claims.

I. PLENARY REVIEW IS WARRANTED BY THE CONFLICTS CREATED BY THE DECISION BELOW AND ITS IMPORTANCE TO THE NATIONAL SYSTEM OF SECURITIES REGULATION

A. The Decision Below Conflicts With Decisions Of Other State Courts Of Last Resort And Federal Courts Of Appeals

This Court has long protected the rights of injured persons to seek relief under state law against fraud and misrepresentations committed by entities whose actions federal agencies heavily regulate. *See, e.g.*, *Bates v. Dow AgroSciences LLC*, 544 U.S. 431, 451-53 (2005). Notwithstanding the parallel or overlapping applicability of federal law, the Court has held that state-law misrepresentation claims are often not preempted, in part because they typically parallel federal duties requiring regulated entities to tell the truth, *see id.*, and because they "rely only on a single, uniform standard: falsity." *Cipollone v. Liggett*

Group, Inc., 505 U.S. 504, 529 (1992) (plurality op.); *see* Pet. 29-30 & n.24. Such claims, therefore, can easily coexist with the federal securities laws that were enacted to ensure full disclosure and thus to protect both investors and the efficient and fair functioning of the securities markets. *See* Pet. 18-19; *Basic Inc. v. Levinson*, 485 U.S. 224, 230 (1988) ("fundamental purpose" of the 1934 Act was to implement a "philosophy of full disclosure") (internal quotation marks omitted).

1. The decision below directly conflicts with *O'Malley v. Boris*, 742 A.2d 845 (Del. 1999), in which the Delaware Supreme Court held that federal law did not preempt a state-law claim that a "negative response letter" from a broker to its customers, although permitted by the SEC-approved rules of the self-regulatory organization NASD, was nevertheless misleading for its failure to disclose the broker's interest. *See* Pet. 20-22

Respondents seek (at 16-17) to distinguish *O'Malley* on the ground that the state suit for misrepresentation did "'not interfere with the purpose or effectiveness of the NASD rule'" at issue, Opp. 17 (quoting *O'Malley*, 742 A.2d at 849), whereas here "the requested disclosures flatly contradict the fact of the SEC's approval as well as the actual language of the [stock borrow program]," *id.* To the contrary, *O'Malley*'s key holding was that federal approval of the NASD rule did not preempt a state-law claim that "additional disclosure requirements . . . [that] would be the same for all [of a broker's] customers" were necessary to avoid misleading investors who received the NASD-approved letters. 742 A.2d at 849. Just so here: there is no inconsistency between the SEC approval that allows the stock borrow

program to operate and a state-law requirement that respondents make disclosures to investors about its operation – or avoid affirmative misrepresentations such as their statement that the program addresses only "temporary shortfalls." *See supra* p. 1.[2]

Respondents further incorrectly suggest that they are helped by *O'Malley*'s discussion of *Guice v. Charles Schwab & Co.*, 674 N.E.2d 282 (N.Y. 1996). They concede, however, that *O'Malley* distinguished *Guice* because "the NASD rule at issue in *O'Malley* did not purport to limit the disclosures which may be included in a 'negative action' letter." Opp. 17. Nothing in the three pages of stock borrow program rules approved in 1981 purports to limit, or even mentions, what disclosures respondents can or must make about the program. If anything, therefore, *O'Malley*'s treatment of *Guice* suggests that the New York court of last resort would agree with *O'Malley*. That does not resolve the conflict demonstrated in the petition, but merely places one more State on petitioners' side of the split. *See* Pet. 23 n.19.[3]

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[2] *See also* Resp. App. 2a (Compl. ¶ 1: ("The Stock Borrow Program . . . was purportedly created to address SHORT TERM delivery failures by sellers of securities in the stock market. However, the end result of the program has been to create tens of millions of unissued and unregistered shares to be traded in the public market. Further, in some instances, the Stock Borrow Program has resulted in two or more shareholders who purchase shares in separate transactions to own the same shares.").

[3] Respondents further argue (at 17) that *O'Malley* is distinguishable because it did not involve allegations that the NASD-approved letters "inherently operated as a fraud." As the petition makes clear (at 15-16), petitioners allege not that the stock borrow program is *inherently* a fraud, but rather that respondents have misrepresented to the public (affirmatively

2. The petition discusses (at 23-26) other cases in conflict with the decision below that respondents address barely, if at all. Those cases show that state-law claims for fraud or misrepresentation rarely conflict with the purpose of federal law because state law almost always furthers federal law by preventing falsehood. Respondents dismiss *Bronco Wine Co. v. Jolly*, 95 P.3d 422 (Cal. 2004) (as well as *Bates*, *see infra* pp. 7-8), as being premised on "Congress's intent in adopting the precise preemption language at issue." Opp. 18. But that distinction makes no difference when the relevant congressional intent is the same. In *Bronco Wine*, the court found that Congress's intent concerning wine labeling was "to protect consumers from misleading labeling, not to permit [such] labeling." 95 P.3d at 457. Similarly here, Congress charged the SEC with exercising its authority under § 78q-1, "having due regard for the public interest, the protection of investors, the safeguarding of securities and funds, and maintenance of fair competition among brokers and dealers, clearing agencies, and transfer agents." § 78q-1(a)(2)(A).[4]

3. Respondents cite (at 18-19) the Seventh Circuit's decision in *American Agriculture Movement, Inc. v. Board of Trade of Chicago*, 977 F.2d 1147 (7th Cir. 1992), as authority for their position on the

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and through omissions) its actual operations. And respondents' argument (at 16-17) that *O'Malley* was a suit against a broker rather than a clearing corporation is an exercise in irrelevancy: both cases involve the preemptive effect on state securities law of the SEC-approved rules of a self-regulatory organization.

[4] Respondents make no attempt to distinguish *Drake v. Laboratory Corp. of America Holdings*, 458 F.3d 48 (2d Cir. 2006), which, as we explain (Pet. 24, 26), also conflicts with the decision below.

merits. If correct, their argument would only deepen the conflict over federal preemption of state securities claims and heighten the need for review. In any event, the case supports petitioners' position (and thus conflicts with the Nevada Supreme Court's decision here) because it states that preemption is appropriate "'only when'" state law is used "'in a manner that would, in effect, regulate [federally regulated] markets'" at the state level. Opp. 19 (quoting 977 F.2d at 1157) (holding that state-law claims for breach of fiduciary duty and negligence were preempted; no mention of any misrepresentation claims). Here, by contrast, holding the clearing companies liable for misrepresenting their business practices to the public would not "directly affect [their] operations," *id.*, but would merely require them to describe those operations accurately to the public – consistent with the shared federal and state policy of full disclosure and candor.

Respondents also point (at 1 n.1, 18) to other district court decisions in their favor on claims involving the same conduct at issue here. Those decisions are of limited relevance to this Court's determination whether to grant review because they involve neither federal courts of appeals nor state courts of last resort, although the widespread litigation over respondents' representations concerning the stock borrow program does help to show that this case involves "an important question of federal law" that should be settled by this Court. Sup. Ct. R. 10(c). In any event, those decisions either followed the erroneous decision below, *see Pet Quarters, Inc. v. DTCC*, No. 4:04-cv-1528-RSW, 2008 U.S. Dist. LEXIS 15316 (E.D. Ark. Feb. 25, 2008), or contained a likewise flawed analysis of the conflict-preemption issues, *see, e.g.*, *Capece*

v. DTCC, No. 05-80498-CIV-RYSKAMP, 2005 U.S. Dist. LEXIS 42039 (S.D. Fla. Oct. 11, 2005); *Whistler Investments, Inc. v. DTCC*, No. CV-S-05-0634-RJC (PAL) (D. Nev. June 1, 2006) (two-page decision adopting *Capece*), *appeal pending*, No. 06-16088 (9th Cir. argued Mar. 10, 2008). A handful of adverse district court decisions is no sure sign of correctness: as this Court noted in *Bates*, it may instead indicate only that "those courts too quickly concluded that [the relevant] claims were pre-empted." 544 U.S. at 446.[5]

B. The Decision Below Conflicts With *Bates*

In *Bates*, the Court made clear that state laws that rest on duties of care congruent with those in federal law are not preempted. *See* Pet. 26-27. *Bates* also compels the lower courts to examine whether state-law remedies would aid the purposes of federal law, and here petitioners' claims would further the fundamental purpose of full disclosure mandated by the securities laws. *See* Pet. 27-30. In addition, *Bates* makes clear that federal approval of regulated activities does not authorize later representations made by a regulated entity in connection with those activities – especially where, as here, the agency has not reviewed those statements. *See* Pet. 30.

In claiming *Bates* to be inapposite (at 18), respondents all but ignore the policy of full disclosure underlying the securities laws. Instead, respondents mistakenly suggest (*id.*) that state-law prohibitions

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[5] Although irrelevant to this case, the summary judgment issued in *Nanopierce Technologies, Inc. v. Southridge Capital Management*, No. 02-CV-0767, 2008 WL 250553 (S.D.N.Y. Jan. 29, 2008), *see* Opp. 4 n.4, in NanoPierce's view left viable breach-of-contract claims that NanoPierce may prosecute.

on misrepresentation are preempted by statutory language referring to "uniform standards and procedures for clearance and settlement." § 78q-1(a)(1)(D). In that very provision, however, Congress declared that "[t]he linking of all clearance and settlement facilities and the development of uniform standards and procedures for clearance and settlement will reduce unnecessary costs and *increase the protection of investors*." *Id.* (emphasis added). Congress could hardly have made clearer its view that § 78q-1(a)(1)(D) was fully consistent with the long-standing federal goal of investor protection, a goal also served by the state laws under which petitioners' claims arise. State laws against fraud and misrepresentation have coexisted with federal securities laws from the beginning, and Congress was careful to include savings clauses in the 1933 and 1934 Acts, as well as the 1975 Amendments. *See* Pet. 9-10.

C. The Petition Raises An Important Issue Meriting This Court's Review

The conflict presented here concerns the interplay of federal and state policies of full disclosure in the securities market, and the decision below interprets federal policy to bar state remedies serving the primary goal of the federal securities laws themselves. Holding the fraud- and misrepresentation-based claims at issue here to be preempted by federal law would be a huge encroachment on the States' long-standing role in adjudicating such claims on behalf of injured parties. *See* Pet. 31.

Respondents (at 20) claim that those policies are not implicated because granting relief to petitioners would subject the clearing companies "to purported state law disclosure obligations that contradict, and therefore obstruct, the federally approved system."

But this argument (which in any event lacks merit) goes to the merits of their case, not to its importance: if petitioners are correct, then the national importance of the federally approved system makes it all the more vital that respondents correctly represent their operations. Further, respondents' purported distinction (at 21) claiming that their clearance and settlement activities come into play only "*after* the trading decisions have been made" simply ignores that the alleged misrepresentations occurred *before* those trading decisions were made and thus affected those decisions.[6]

Further, respondents rely (at 4) on the fact that the alleged misrepresentations and omissions affected numerous companies and were not limited to petitioners here. But that makes the issue presented

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[6] Respondents incorrectly claim (at 3) that petitioners' position is "wholly contrary to the SEC's own characterizations and assessment [of the stock borrow program] in approving the program pursuant to its Congressional mandate." Respondents do not dispute that the SEC in the end *agrees* with petitioners' fundamental allegations regarding the existence of phantom shares in the market. *See* Pet. 18 n.16. The controversy in this case is whether they should be liable for misrepresenting the existence and extent of those phantom shares, including but not limited to respondents' statements that such conditions are merely "temporary" when in fact they are persistently long-standing. *See supra* pp. 1, 4; *see also* Helen Avery & Peter Koh, *The Curious Incident of the Shares That Didn't Exist*, *Euromoney*, Mar. 2005. Relatedly, respondents attempt to obscure, but do not dispute, that their mode of operation of the stock borrow program permits the DTC member broker for the buyer of loaned shares to re-lend those shares, which can result in numerous "owners" of the same shares and is not disclosed to the investing public. *Compare* Pet. 14-15 (explaining this) *with* Opp. 11 (stating only that the original lending broker cannot re-lend the same shares but not addressing the buying broker's ability to do so).

more important, not less. This Court should soon address the far-reaching harm caused by respondents' conduct, permit state law to provide a remedy for the numerous companies and investors that respondents have injured, and protect the integrity of the national securities markets.

II. IN THE ALTERNATIVE, THIS CASE SHOULD BE HELD PENDING THIS COURT'S DECISION IN *ALTRIA*

In the alternative, the Court should hold the petition pending its decision in *Altria Group, Inc. v. Good*, No. 07-562. *See* Pet. 32-33. Respondents suggest (at 21) that the issue there is limited to "express preemption." But the Court granted certiorari on questions of both express and implied preemption.[7] Moreover, the petitioners' brief in that case (at 45-57 (filed Mar. 31, 2008)) argues an implied preemption theory, claiming that a "state-law challenge to the use of FTC-authorized descriptors would substantially impede the FTC's low-tar policy." *Id.* at 46. It is therefore possible that the Court could address implied preemption in a way that will be instructive to the lower courts in this and similar cases. Accordingly, if the Court chooses not to grant review at this time, it should hold this case pending a decision in *Altria*.

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[7] *See* http://www.supremecourtus.gov/qp/07-00562qp.pdf. The Court has also granted certiorari on an implied preemption issue in *Wyeth v. Levine*, No. 06-1249. That case raises an issue of implied preemption by Food and Drug Administration actions of claims brought against a pharmaceutical maker. *See* http://www.supremecourtus.gov/qp/06-01249qp.pdf. In light of the possibility that the Court may not reach the implied preemption issue in *Altria*, the Court may consider it appropriate to hold this case for *Wyeth* as well.

CONCLUSION

For the foregoing reasons and those stated in the petition for a writ of certiorari, the petition should be granted.

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